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AUGUST 13TH–19TH 2005

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Goodbye to Gaza

Aug 13th 2005

Israel's disengagement from the Gaza strip, which is due to start next week, will lead nowhere unless George Bush re-engages in Palestine ... more

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Politics this week

Aug 11th 2005
From The Economist print edition

The lion's last roar?

Junichiro Koizumi, the prime minister of **Japan**, called a snap general election after losing a key vote authorising the privatisation of the country's postal service, which because of its savings and insurance businesses is the world's largest financial institution.

See article

Japan and the world commemorated the 60th anniversary of the nuclear bombings of **Hiroshima**, on August 6th, and **Nagasaki**, three days later. Around 210,000 people were killed outright by both bombs; a further 100,000 died over the years from radiation-related illnesses.

AP

Six-party talks on the crisis caused by **North Korea's** pursuit of nuclear weapons broke up without agreement in Beijing after 13 days. But the negotiators hope to resume work on August 29th, and America's lead negotiator said the North Koreans had shown a “seriousness of intent”.

See article

In **India**, an inquiry blamed local Congress party politicians for inciting riots, in which an estimated 3,000 people died, directed against Sikhs following the assassination of Indira Gandhi in 1984 by her Sikh bodyguards. A minister has resigned.

See article

Rowing over money

Rafael Correa quit as **Ecuador's** finance minister after disagreements with President Alfredo Palacio over Mr Correa's plans to borrow up to $300m from Venezuela, and with the World Bank, which has suspended a $100m loan.

Two leading contenders in **Mexico's** presidential race, Roberto Madrazo of the PRI and Santiago Creel of the PAN, suffered blows as polls showed internal rivals catching up with both men.

See article

Ireland said it would consider a request by **Colombia** to jail or send back three suspected members of the Irish Republican Army who jumped bail and fled home while facing accusations of teaching leftist FARC guerrillas to make bombs.

A judge investigating the finances of Chile's ailing ex-dictator, **Augusto Pinochet**, ordered the arrest of his wife and youngest son over tax-fraud allegations.

A commission of lawmakers recommended lifting the immunity of **Nicaragua's** President Enrique Bolaños so that he can be prosecuted on election-fraud charges. The row over the allegations has held up Nicaragua's ratification of the CAFTA trade deal.

In **Brazil's** biggest bank robbery, thieves tunnelled into the Central Bank's branch in the city of Fortaleza and grabbed 156m *reais* ($68m).

Fidel Castro's government cheered as an American appeals court overturned the 2001 convictions of five

alleged **Cuban spies**. Cuba says they were spying only on anti-Castro groups, not on the United States.

On a wing and a prayer

The American space shuttle **Discovery** returned safely from its two-week mission. However, the landing was delayed and the location moved to California because of bad weather in Florida. NASA has grounded all shuttle flights because of safety concerns, and scientists wonder if the programme will ever get off the ground again.

John Paul Stevens, a Supreme Court justice, criticised the **death penalty**, saying a substantial number of sentences had been “imposed erroneously”. He insisted the issue should be prominent at next month's confirmation hearings for John Roberts, George Bush's nominee to the court.

Jeanine Pirro, a Republican district attorney from Westchester county, announced she was entering the field to run against Hillary Clinton in next year's **New York** senate election. Tipped to win the Republican primary, Ms Pirro is a moderate who supports abortion rights and presents a tougher challenge than Mrs Clinton would have wanted.

The Census Bureau reported that, thanks to a continuing influx of Latinos, **Texas** has become the fourth state in America to have a majority non-white population.

Breaking the seal of approval

Iran rejected proposals from Britain, France and Germany for economic incentives and security guarantees in return for an indefinite suspension of its uranium-reprocessing activities that might enable it to make a nuclear bomb. Instead, it broke the seals in a uranium-conversion facility at Isfahan where the suspension had been in force. The International Atomic Energy Agency began discussions on whether Iran should be referred to the UN Security Council. America and others want to impose economic sanctions.

See article

Israel's finance minister, Binyamin Netanyahu, resigned in protest against the impending withdrawal of Israeli forces and settlers from the Gaza strip, arguing that nothing would be gained in return. He is likely to bid for the leadership of the ruling Likud party against the current prime minister, Ariel Sharon.

See article

In the first cabinet meeting of his new reign, King Abdullah of **Saudi Arabia** pardoned three liberals arrested 18 months ago for calling for a constitutional monarchy, and freed several Libyans imprisoned on suspicion of trying to assassinate him. The American and British authorities told their citizens in the kingdom to watch out for terrorist attacks against them.

Playing by the rules

Germany's Constitutional Court began deliberations on whether the early general election called by Chancellor Gerhard Schröder should be allowed. The court's decision, likely to come at the end of the month, is the last hurdle before the election can be held on September 18th.

See article

Milan Lukic, a **Bosnian Serb** wanted for war crimes committed in 1992, was arrested in Buenos Aires and is expected to be sent to The Hague war-crimes tribunal. Despite myriad rumours of their imminent capture, the two most-wanted Bosnian Serb leaders, Ratko Mladic and Radovan Karadzic, remain at large.

Relations between **Poland and Russia** came under strain after a second Polish diplomat was beaten up in Moscow. The spat began a few weeks ago when Russian children were attacked in a Warsaw playground, and Russia demanded an apology.

A **Russian mini-submarine** trapped off Kamchatka was cut free by a British

AFP

naval robotic submarine, provoking argument in Russia both over who was to blame for an incident reminiscent of the *Kursk* disaster in 2000 and over reliance on foreign assistance.

See article

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Business this week

Aug 11th 2005
From The Economist print edition

Utilities merger

Suez, a French utility group, launched an *euro*11.2 billion ($14 billion) bid to buy the 49.9% of **Electrabel**, Belgium's biggest electricity operator, that it does not already own. The move follows a recent wave of consolidation among European utilities that are seeking to maximise profit from higher energy prices.

See article

German regulators may need several months to approve the takeover of **ProSiebenSat.1**, a broadcaster that controls around 45% of Germany's TV advertising market, by **Axel Springer**, the country's largest newspaper publisher. The deal, valued at *euro*4.2 billion ($5.2 billion) was announced last week, but politicians worry that the merged company will be too powerful.

See article

A judge ruled in favour of **Walt Disney's** directors and said they acted in good faith when appointing Michael Ovitz president in 1995. Mr Ovitz was sacked a little over a year later with a compensation package valued at some $140m. Shareholders brought the lawsuit against Disney last year. It was regarded as a test of how far a firm's directors were personally liable for bad board decisions.

See article

A fair exchange

Yahoo! agreed to pay $1 billion in cash for a 40% stake in Alibaba.com, a leading Chinese e-commerce firm. As part of the deal, Alibaba will also take over Yahoo!'s operations in China.

See article

Lenovo reported its first quarterly result that incorporates the acquisition of IBM's personal-computer business. The Chinese firm's net income was HK$357m ($45.9m) for the three months ending June 30th, a 6% rise on a year earlier. Sales soared to HK$19.6 billion, from HK$5.9 billion.

Intel revealed that it was being investigated by South Korea's Fair Trade Commission for its marketing and rebate schemes to computer manufacturers in the country. The world's largest chipmaker faced a similar probe in Japan earlier this year and is currently the subject of an antitrust investigation by the EU.

Microsoft settled a lawsuit against **"spam king"** Scott Richter for $7m. The case was brought against Mr Richter and his company in December 2003 as part of an effort to cut back unsolicited e-mails. Mr Richter also agreed to comply with the American government's CAN-SPAM act.

See article

Rupert Murdoch's **News Corporation** extended its poison pill for a further two years, as negotiations stalled to buy the 18% stake in the firm held by John Malone's Liberty Media.

E*Trade, an online broker, said it was buying **Harrisdirect**, a rival, for $700m. The deal provides some consolation for E*Trade, which failed in its effort to take over Ameritrade earlier this year.

Cisco Systems, the world's biggest maker of internet networking equipment, reported a 30% rise in

net income, to $5.7 billion, for the year to July 30th. John Chambers, Cisco's boss, scotched press rumours that the company was about to launch a bid for **Nokia**.

Fasten your seatbelts

Shares in **Delta Air Lines** fell sharply as the troubled firm delayed an SEC filing while it negotiates a new contract with credit-card processors. America's third-biggest carrier has lost $10 billion since 2001 and its share price has fallen by half in the past month.

China revealed the currencies in its currency basket being used to manage the revalued **yuan**. The dollar, euro, yen and Korean won predominate, but other currencies, such as the Russian rouble, are also included. No details were given on the weights given to each currency.

See article

Unocal's shareholders formally approved Chevron's $18.3 billion takeover of their oil and gas firm, ending a four-month battle for control which resulted in defeat for CNOOC, a big Chinese state-controlled oil firm.

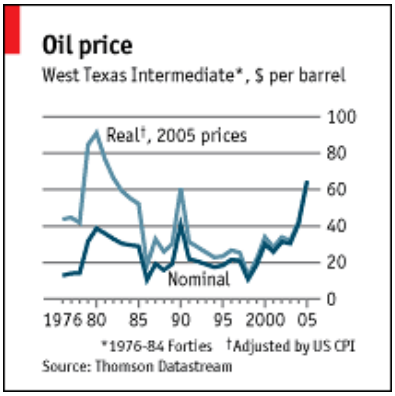
Kerr-McGee, an oil and gas firm based in Oklahoma City, sold its British North Sea assets. **A.P. Moller-Maersk**, the world's largest container-shipping company, will buy the bulk through its energy subsidiary, which wants to expand out of Denmark's fields, for $2.95 billion. **Centrica**, British Gas's parent company, will pay $566m for the rest.

In what appeared to be a bid to boost investor confidence, Russia reduced its claim for back taxes against **TNK-BP**, BP's Russian joint-venture, to $247m. A bill for almost $1 billion was unexpectedly delivered in April.

Back to the eighties?

Oil prices pushed above $65 a barrel on renewed fears of Middle East security. A large fire at a refinery also made traders nervous about oil supplies. Consumers continued to feel the effects of high prices: unleaded petrol jumped by eight cents to an average of $2.37 a gallon in America.

See article



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Letters

Aug 11th 2005
From Economist.com

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

Tackling AIDS

SIR – You dismiss the ABC (Abstinence, Be faithful, Condoms) approach to AIDS prevention as "a slap in the face to many" ("Too much morality, too little sense", July 30th). The logic you imply seems to be that if abstinence or faithful behaviour are not feasible for some people (prostitutes, in this case), then they should not be options for anyone. You also assure us that "condoms are the best prophylactic available", yet there is no evidence that more condoms equals lower infection rates among Africans, as a 2003 UNAIDS study concludes.

Evidence for the effectiveness of condoms in reducing HIV rates comes from places like Thailand and Cambodia, which have different types of epidemic patterns than Africa. When HIV infections are concentrated among sex workers, it is feasible to promote condoms; prostitutes and their clients will use them. However, few people use condoms consistently outside high-risk groups—and the vast majority of Africa's HIV infections occur outside such groups.

Edward Green
Harvard Centre for Population and Development Studies
Cambridge, Massachusetts

SIR – You argue that "The lesson for rich and poor alike is that to contain AIDS morality must take second place." This is wrong. Morality must always take first place. That is why the immoral pandering of the Bush administration to the religious right should be opposed all the more. No moral code, and certainly not the Christian one, condones condemning millions of people to death on such trivial grounds as use of a condom.

Iain Martel
Toronto

Don't mention the war

SIR – Your obituary of General Westmoreland repeats the myth that Vietnam was America's first and only defeat (July 30th). In fact, it was the second. The United States declared war on Britain on June 18th 1812 because the Royal Navy was interfering with its trade and had pressed sailors from American ships. Confident that Britain had its hands full with Napoleon in Europe, America struck at Canada, the acquisition of which would be "a mere matter of marching" according to Thomas Jefferson. After Napoleon was exiled to Elba, freeing seasoned British regulars who began to pour across the Atlantic, America was glad to look for peace. The Treaty of Ghent gave no recognition to either free trade or sailors' rights, which were the *casus belli*, and Canada was left intact and British. Sounds like an American defeat to me.

David Gorrell
Niagara-on-the-Lake, Canada

Cooling the dragon's breath

SIR – You propagate the canard that, economically, China now rules the world ("From T-shirts to T-bonds", July 30th). It does nothing of the kind. In real dollar terms (purchasing-power parity valuations are at best controversial, at worst misleading) China has made a continuously declining contribution to global GDP growth from 10% of the total growth registered in 2001 to an estimated 6%

in 2004—its share of real global GDP was an estimated 2.2% for 2004. There is also some quantitative flaw in your argument that cheap Chinese exports kept global inflation down, as China's share of global trade (an estimate unencumbered by PPP considerations) stood at 6.6% of global exports and 6.2% of global imports in 2004.

It is the speed of the rise of China's share in global economic and trade flows, as well as the growth of its demand for commodities, that has obscured the fact that China consumes, for example, less than 10% of the global output of oil. So what is truly special about China? Its average position in the scheme of things is still very small, although its absolute speed of growth and its opening economy are a harbinger of growth to come. But all of this is a far cry from controlling the world economy.

Andrew Freris
Chief economist, Asia-Pacific
BNP Paribas
Hong Kong

Middle East priorities

SIR – Your report on George Bush's policy towards the Middle East ignores the pressing material needs of people in the region, which must be addressed before democracy can occur ("Does he know where it's leading?", July 30th). Alleviating poverty is one such need. Even though many countries in the region are classified as "middle-income", economic distribution is highly skewed. Moreover, a number of trends are converging to act as protracted time bombs: water is increasingly scarce, a problem exacerbated by climate change; the region is already the biggest grain importer in the world; and the demographic bulge is swelling by the year. Mr Bush should tackle such issues ahead of his obsession with democratic reforms that will, in any event, take too long to prevent the dangerous consequences of economic failure.

Richard Thomas
Aleppo, Syria

SIR – The flaw in America's vision for the Middle East is that it conflates democracy and liberalism, which do not have any natural relationship. As the more theocratic ideas for the Iraqi constitution, the election of Mahmoud Ahmadinejad in Iran, and the recent passage of the "Taliban law" in Pakistan's North-West Frontier Province illustrate, Muslim countries may want to choose their leaders, but they do not necessarily want to accept the liberal values of modern societies in the West. Mr Bush may be thwarted in his efforts by the West's propensity to assume a universal franchise means universal freedom.

Edmund Rogers
Cambridge, Cambridgeshire

Accounting for change

SIR – The problem about asking companies to publish the assumptions underlying their accounts is knowing how to interpret them, and understanding the interaction between them ("Crooks and books", July 30th). It would be far better for chief financial officers to offer us "three-dimensional accounts" made available online. The reader can then hit a key and switch from historical cost to fair value, from FIFO to LIFO, and so on. The quantity of additional work would not be great since most of this information is already prepared. However, the impact could be immense, particularly on self-knowledge within the firm, and deceit would become difficult, as it is likely to be more obvious under one set of assumptions or another. A company's finances are like statues, which one can properly appreciate only by walking around.

Will Hopper
Chairman, W.J. Hopper & Co
London

SIR – You say "It is every boss's job to make his firm's profits look as good as possible." This would be correct if you left out the word "look". The desire to make things "look good", rather than "be good", is the kind of mental fiddle that provided the backdrop to recent financial scandals, and to which accounting reforms are now responding.

Vance Koven
Boston

SIR – My professor on an accounting course at Harvard Business School 25 years ago introduced it thus: “When most of you read accounting statements now, you do not understand them. At the end of this course, you will not believe them.”

Damianos Damianos
Athens

ONLINE ARTICLES

The following correspondence refers to articles published only online

Schrempp and DaimlerChrysler

SIR - Sometime in the late 1990s a slick TV commercial ran hailing the birth of DaimlerChrysler ("Schrempp runs out of road", Economist.com, July 28th). The images of a whole fleet of vehicles, from tiny cars aimed at 18-year-old first owners to luxury sedans for business executives, sports cars for entrepreneurs and commercial vehicles for fleet buyers, all swept majestically across a dry salt lake at sunrise. All these different brands for different consumers mixed up in one stable, under one brand.

Perhaps the business logic was sound, but the mixing of consumer brand values and corporate culture was never going to work. A Chrysler with Mercedes technology is one thing, but a Mercedes with Chrysler reliability is another thing entirely. The resulting confusion has put Mercedes behind Lexus and BMW, damaged brands that have taken decades to build and destroyed shareholder wealth. Where were the chief marketing officers during the decision-making process?

Kevin Moore

Bush's Supreme Court nominee

SIR - You refer to "blacks, gays, and abortion-rights supporters" as "special-interest groups" ("A stealth nominee flies into enemy territory", Economist.com, July 20th). It would be more accurate to characterise these groups as segments of American society whose interests tend to conflict with the platform of the Republican Party.

Aidan Carter

Buttonwood on tech stocks

SIR - Buttonwood's recent column ("Another tech-stocks bubble?", Economist.com, July 22nd) stated: "The price of Google's traded shares implies that the firm is worth some $84 billion, which would make it the biggest media company in the world...comfortably in excess of Time Warner's $76 billion." Differing capital structures mean it may not always be right to compare equity market capitalisation. Since Time Warner is loaded down with debt but Google has none, implied enterprise value is more relevant. Time Warner has balance-sheet assets of $121 billion. The group's debt of $57 billion and its market capitalisation of $76 billion imply that the market values these assets at $133 billion. This doesn't argue that Google is cheap, though, and of course bigger is not always better.

D. Nowakowski

SIR - It seems that the ever-increasing demand for the internet is impervious to the cyclical shocks of the economy. Companies such as Google can endure bad economic times by continuing to innovate and keep their multitude of users happy. Of course, it remains to be seen how long companies like Google can continue to innovate.

Balkrishna Rao

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Leaving Gaza

Goodbye to Gaza

Aug 11th 2005
From The Economist print edition

Israel's disengagement from the Gaza strip will lead nowhere unless George Bush re-engages in Palestine

AFP

CUI BONO (who benefits?) is said to be a helpful question to ask when you are trying to unravel a mystery. Yet it does not tell you much about why Ariel Sharon intends next week to start pulling all of Israel's settlers and soldiers out of the Gaza strip, which it has occupied for more than a generation, since the war of 1967. Some Palestinians say that only Israel will benefit. Some Israelis say that only Palestinians will benefit. The true answer in this case is that who benefits depends almost entirely on what happens next—and nobody has much of a clue about what is going to happen next.

What it isn't

Mr Sharon's "disengagement" plan is a mystery because of what it is not. It is not the product of a peace agreement. Instead of land for peace—the principle under which Israel returned Sinai to Egypt in 1982—Israel is quitting Gaza pretty much unilaterally, after minimal co-ordination with the Palestinians, and with no firm promise that their ferocious *intifada* will not erupt again the moment the settlers have gone. Nor is the plan necessarily a step towards an independent Palestinian state, since it includes only a token withdrawal from the much bigger West Bank, which would have to be the heart of any Palestine worth the name. So just as the Israelis cannot be sure that the *intifada* won't resume, the Palestinians cannot be sure that Mr Sharon does not intend after leaving Gaza to sit tight everywhere else (see article).

Oddly enough, given that this is an Israeli initiative, the only people who in the short run are almost certain to benefit are the Gaza strip's 1.3m Palestinians. Israel's 8,000 or so settlers have occupied more than a fifth of the scarce land in the strip. During the *intifada*, protecting the settlers required Israel to keep military forces in Gaza, who killed plenty of innocent civilians while fighting Palestinian gunmen and suicide bombers. So even if Israel's departure is not followed—as it should be—by massive economic help, the departure of all Israel's settlers and soldiers will improve life in the strip.

What does Israel stand to gain? Nothing at all, cry Mr Sharon's many detractors at home. Binyamin Netanyahu, the former prime minister who resigned this week as Mr Sharon's finance minister, speaks for most of Israel's Likud party when he foresees nothing but negatives. Even Israelis who support the principle of land for peace are troubled about giving up land with no peace deal in return. They say that this will embolden the Palestinians' men of violence, who already boast that it was their attacks that

made Israel flee, and who will now use both Gaza and the West Bank as a haven from which to launch more rockets and suicide bombers into Israel proper.

What may happen next is therefore that the conflict will revert to its previous stalemate. The Palestinians will resume their attacks, asking how else they can throw off the occupier. Israel will say that it cannot give up more land until the Palestinians give up terrorism. It will be back to square one—except that Israel will have surrendered the square called Gaza. But in that event not even the Palestinians will benefit much, because if the *intifada* does resume Mr Sharon will send Israel's tanks and helicopters straight back in—unencumbered this time by the complication of protecting the settlers.

After decades of false dawns, those who expect little from the Gaza disengagement have experience on their side. That may include its architect. For all anyone can tell, Mr Sharon's true aim is to fight on from shorter lines, having earned credit with America by sacrificing Israel's most dispensable settlements, all for the sake of holding tighter to the big ones in the West Bank. Sitting tight will probably lose Mr Sharon the support of his Labour coalition partners, and so bring an early election, but few expect Labour to win it. The likely outcome—after diplomacy has been stalled by months of electioneering—is Likud again, under the tough Mr Sharon or the no less tough Mr Netanyahu, with little change in policy.

What it could be

Must it be like this? If disengagement is to be more than an interlude, the next big job after the settlers leave must be to prevent the war of attrition from resuming. In the “road map” which both Israel and the Palestinians have signed this is the job of the Palestinian Authority. But the PA was a feeble thing even before Yasser Arafat's death last November, and Mahmoud Abbas, his successor, has neither the willpower nor the firepower to stop the extremists of Hamas from resuming the fight if they so choose. He needs help—though it has to be help of the economic and political, rather than the military, sort.

Why economic? Mr Abbas may not be able to stop Hamas from resuming the *intifada*, but the Palestinian people can. And they would have a good reason to do so if the disengagement brought a big improvement in their lives, which they believed a return to violence would jeopardise. Outsiders can help in this: James Wolfensohn, the former head of the World Bank, is trying to organise a post-disengagement dividend for Gaza. But it is still Israel that can do most to improve the economic lot of the Palestinians: not only in Gaza, where it will continue to control the flow of people and goods across the border, but also in the West Bank, which despite the ceasefire remains under a harsh regime of closures and roadblocks.

Beyond economics, the Palestinians need a “political horizon”—a believable promise that George Bush's oft-enunciated “vision” of a viable Palestinian state in the West Bank as well as Gaza is achievable without recourse to the gun. That state cannot come instantly: the two sides are farther apart today than they were when Bill Clinton's peacemaking efforts collapsed in 2000, and trust each other less. But with America pushing, it should at least be possible to start a process, building first on self-government for Gaza and, in the West Bank, a settlement freeze followed by further withdrawals. Israelis and Palestinians are exhausted after five years of violence, and susceptible to pressure. Wary of failing as Mr Clinton did, distracted by Iraq, and reluctant to lean on Israel before it got out of Gaza, Mr Bush has kept his distance. The day after Mr Sharon pulls out must be the day that Mr Bush steps in.

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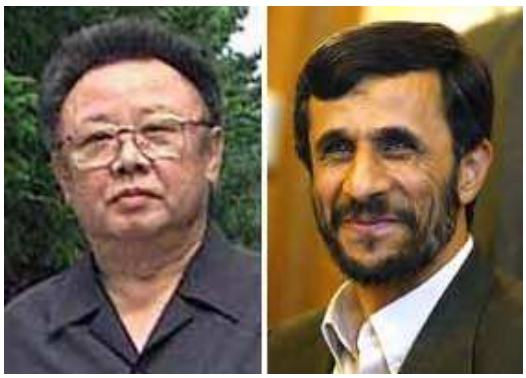
North Korea and Iran

Too late to stop their nukes?

Aug 11th 2005
From The Economist print edition

China may be better placed than the West to do some last-ditch dissuading

Reuters AFP



IT HAS been a rocky week for those who fear that nuclear weapons in the hands of particularly nasty or nutty regimes pose the biggest threat to the planet's future. Almost simultaneously, the two surviving regimes in George Bush's "axis of evil", North Korea and Iran, have poked the de-nukers in the eye by spurning the latest goodies offered to dissuade them from making, or being able quickly to make, nuclear bombs. The offers included economic incentives (in North Korea's case to stave off the hunger and cold that threaten its miserable people in winter) and security guarantees (in Iran's case, implicit ones) that America would no longer seek "regime change", if not through the ballot box then by darker means. But if both regimes say boo to the rest of the world, what next?

The biggest worry is that nuclear weapons will proliferate, especially in countries that might, in turn, pass them on to terrorists and other undesirables. If Iran's mullahs find the means to make a bomb fast, Saudis and Egyptians may be tempted to follow suit. If North Korea, which hints it already has a rudimentary bomb (maybe half a dozen of them), were to test one, Japan might be tempted to match it. And so on.

In truth, there is not much, in the short run, that anyone can do to stop this ghastly sequence, though an Israeli military strike against Iran's scattered nuclear facilities cannot be ruled out: the Islamic Republic is the region's only country that steadfastly refuses to accept Israel's existence. But that might set back Iran's nuclear ambitions by only a year or two. In any event, the United States is much more reluctant than before to let anyone, especially Israel, enrage Iran's ruling mullahs, who could easily stymie America's desperate efforts to create a new order next door in Iraq.

If Iran goes ahead, as this week it said it would, and starts to convert uranium yellowcake into UF-4, the first stage towards enriching it for a bomb-making fuel cycle, the next step is for the UN's nuclear watchdog, the International Atomic Energy Agency, to refer Iran to the UN Security Council, with a view to imposing economic sanctions on Iran.

North Korea's case is a bit different. Only last month, after a 13-month sulk, did it return to six-country negotiations with China, Japan, Russia, South Korea and the United States. The hope is that it will be persuaded by huge dollops of aid, especially food and electricity, and by an American promise that it will not seek regime change, to forgo its bomb, however much North Korea's paranoid leader, Kim Jong Il, loves having one.

China's chance—or obligation

The country that links both would-be nuclear bomb-wielders is China. It does not want North Korea's regime to collapse, for fear of the ensuing spillover. Nor does it want nuclear weapons to proliferate in the already twitchy Korean peninsula or, worse in Chinese eyes, in Japan. And China has most leverage over North Korea: it could, literally, switch its lights off. China's role in Iran has grown too. It expects to buy oodles of Iranian oil and gas. Iran, which has co-operated with North Korea over missiles, may be betting that China (if not Russia) would veto a Security Council resolution demanding sanctions if it refused to curb its nuclear ambitions. China wants to be acknowledged as a responsible and weighty voice at the nuclear countries' top table. In that case it should try harder to make its Iranian and North Korean friends see sense and desist from making, or holding on to, their nukes.

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Terrorism

Dealing with traitors

Aug 11th 2005
From The Economist print edition

The British government's anti-terrorism proposals are wrong, both in principle and in practice

MEPL

"LET no one be in any doubt: the rules of the game are changing." Even by Tony Blair's demotic standards, it was a stark response to last month's bombings in London. Outlining on August 5th what he described as a "heavy agenda" of 12 reforms to Britain's immigration and criminal justice systems, Mr Blair opened a new front in the war on terror. Battle will now be joined not just with terrorist plotters, but also with the extremists who inspire them (see article). If the prime minister gets his way, any foreigner who indulges in extremism, even if he does no more than run an unsavoury bookshop or website, will be deported. Naturalised Britons will be stripped of their citizenship before being treated in the same way. Troublesome outfits will be proscribed and their meeting places shut.

Quite right too, said the Conservative opposition and many of Britain's newspapers. They want to see the back of men like Omar Bakri Mohammed, the former leader of the now dissolved Islamist group al-Muhajiroun, who has insisted that Muslims cannot be blamed for the London bombings or the attacks on America. Nods of approval also came from France, which already takes a tough line on the deportation of inflammatory preachers and plans to speed up the exodus in the next few months (see article). The French disapprove of what they regard as an absurdly sensitive attitude to free speech in Britain—and resent it, too, since at least one man who they believe was involved in bombings in Paris a decade ago took refuge in "Londonistan".

Britain's anti-terror laws are among the toughest in the world—not surprisingly, given the long struggle against the Irish Republican Army. But the legal system is not so tough on inflammatory speech, unless it happens to be directed at a racial group. Although bringing firebrands to book is possible under incitement and conspiracy laws, it means proving a direct link with criminal acts, which is tricky. Evicting foreign preachers is also difficult. That is not so much, as is often claimed, because the European Convention on Human Rights has been incorporated into British law, but because of the country's adversarial legal system, together with a long history of sheltering troublemakers who do not propose to carry out their plans on British soil. "Londonistan" existed long before the Human Rights Act.

Trust us

There are two good arguments for lowering the threshold for prosecution and deportation. The first and most obvious is that extremism is the pool in which terrorists swim: it inspires, supports and justifies them. Those who watch would-be terrorists say that radicalisation often begins with a chat with a charismatic agitator, although the sort of loudmouths who give interviews to newspapers are much less dangerous than the covert kind. Curtail offensive speech and the number of potential bombers might fall. The second reason is that extremism creates fear and resentment. Because they are liable to cause a backlash, fiery Islamist clerics pose more danger to western Muslims than to anybody else.

These arguments are seductive at a fearful time, yet they must be resisted. The prime minister's proposals would serve the terrorists' ends by undermining the civilisation they attack. Free speech is not a privilege, to be revoked if it is misused, but a pillar of democracy. Threatening naturalised citizens with deportation if they flirt with extremism, as the government intends, will create two classes of citizen: the British-born and the rest. That will do incalculable harm to race relations and undermine the inclusive British identity that Labour has tried to nurture.

The government's proposals may also achieve the opposite of what is intended by further alienating

Britain's Muslims from their fellow countrymen. Many say that, since the attacks on London, they feel under suspicion. Now they fear that they will be punished for the sort of violent speech that might be overlooked if it was, say, uttered by a drunken football fan. For an indication of how far trust has already broken down, compare the reaction to the bombings of July 7th and that to the announcement of August 5th. A month ago, mainstream Muslim leaders stood alongside politicians and promised to co-operate in the struggle against home-grown terror. But since Mr Blair revealed his latest proposals, they have dug in their heels even against the banning of extremist organisations that they formerly attacked.

The government says it will use the new powers it plans to acquire with restraint. Trust us, it implies: only nasty Muslims will be targeted. Everybody else can relax. But even if a government could be trusted to keep such a promise, which none can be, it should not be accepted. Laws are not created in order that undesirables may be put away. That is a side effect. Their real purpose is to set down clear guidelines about what is acceptable and what is not.

Mr Blair is right that things are changing. People are scared, and are therefore more inclined to trust government than they normally would. That's dangerous. The sooner Britons' healthy wariness of government returns, the better.

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Italian banking

Please go, Mr Fazio

Aug 11th 2005
From The Economist print edition

Antonio Fazio, the governor of Italy's central bank, should resign or be sacked

AP

CENTRAL bankers have a difficult job. Their effectiveness depends on integrity and discretion, notably on monetary policy but also on issues of banking supervision. Most are sober and careful. The few that have cast doubt on their integrity by stumbling have resigned quickly. What to do, then, when a central banker behaves with such wilful disregard for ethical standards that he ought to resign, but shows no sign of doing so, or even of feeling a smidgen of embarrassment?

That is the dilemma facing Italy. The Bank of Italy, its central bank, has enjoyed some respect at home and abroad—until recently. Along with the Treasury, it oversaw Italy's entry into the euro. Several banking messes were effectively dealt with, so that Italy can now point to some well-capitalised and well-run banks that are beginning to modernise the country's old-fashioned financial industry. For that, Antonio Fazio, the central bank's governor, deserves credit. Appointed for life on a fat salary in 1993, he showed a streak of independence that largely freed his bank from suspicions that it could be influenced by politicians. That made it something of a rarity among Italian public institutions.

Lately, however, Mr Fazio has undone his good work. First there was his disappointing response to the Parmalat scandal, in which domestic and international banks were directly implicated. After the dairy firm collapsed in late 2003 in Europe's biggest case of corporate fraud, sensible regulatory reforms were suggested by Italy's finance minister. But some of these involved narrowing the Bank of Italy's broad powers. So Mr Fazio used all his influence to brush these useful reforms away or to water them down. This was an ominous sign.

Much worse was to come. When two foreign banks, one Dutch, the other Spanish, launched contested takeover bids this year for a couple of Italy's smaller banks, Mr Fazio pretended that normal scruples would govern the outcome. He publicly denied the accusation that he had a “fortress Italy” mentality. Behind the scenes, however, he intervened blatantly again and again to favour rival Italian bids.

This was especially the case in the battle between the poorly capitalised Banca Popolare Italiana (BPI) and ABN Amro to win control of Banca Antonveneta, Italy's ninth-biggest bank. And it is his conduct in this deal that makes him unfit to remain in his job. Despite serious doubts among his own officials, Mr Fazio seems to have been determined to engineer a reverse takeover of Antonveneta by BPI and to thwart the Dutch bid. But this was possible only by ignoring allegedly illegal and underhand manoeuvres by BPI that led recently to the suspension of its boss, Gianpiero Fiorani, and of the bid. Mr Fiorani is a close friend of Mr Fazio's—so close, in fact, that the central banker personally telephoned Mr Fiorani late

at night last month to tell him that he had approved BPI's bid. That phone call, along with many others, was tapped by magistrates who suspected that BPI was systematically breaking the rules and had placed Mr Fiorani under surveillance.

Details of how BPI twisted and inveigled its way to control of Antonveneta make disturbing reading (see article). So does evidence that a group of businessmen linked to BPI might be trying to wrest control of politically sensitive assets that include *Corriere della Sera*, one of Italy's most respected newspapers. But perhaps most disturbing is that Mr Fazio seems to believe that he has done nothing wrong. The Bank of Italy has issued a statement claiming that its managers have acted properly and legally.

Ciampi's task

It is not yet clear whether or not Mr Fazio has broken the law—in his position the rules allow him a great deal of latitude. But it is already clear that he has not acted prudently or ethically and has, in fact, damaged the Bank of Italy badly. Despite this, Silvio Berlusconi's government has done nothing, and is apparently willing to see the Bank's authority wither. This is a grievous lapse that is not in the country's interest. There is one hope. Carlo Ciampi, Italy's president, was himself once governor of the Bank of Italy and understands the institution's importance. He has the moral and political authority to force Mr Fazio out. He should use it.

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Monetary policy

All at sea?

Aug 11th 2005
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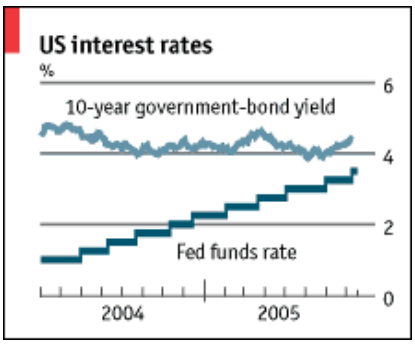
The Fed's interest-rate rudder isn't working



ALAN GREENSPAN, chairman of America's Federal Reserve, has often been called “the most powerful man in the world”, and those who think of him this way have not been joking. He is, indeed, the mightiest of the world's central bankers, an influential group by any measure. But lately Mr Greenspan has seemed not powerful but impotent. This week the Fed under his direction raised interest rates for the tenth time since June 2004. And yet monetary policy is no tighter than it was—thanks to lower bond yields.

Central bankers are often viewed as drivers or pilots of their national economies. Commentators urge them to put their foot on the accelerator, to tap the brakes, or to aim for a soft landing. Yet in reality they have more in common with early sea-faring navigators. Like them, central bankers lack reliable maps and compasses. Because of statistical lags and huge uncertainty they do not know where the economy is today, let alone where it is heading. Some of the policy dilemmas they face (eg, whether they should try to prick a housing bubble) are the equivalent of not knowing whether the Earth is flat or round. Now on top of this, today's “navigators” have a big new problem: their interest-rate rudder appears to have jammed.

Judged by the obsession of financial analysts and newspapers with the meetings of the Fed's key policymaking committee, one would conclude that America's federal funds rate is the most important price (ie, of money) in the world. Yet it matters less than most people believe. Economies are driven by overall financial conditions, which also depend on long-term bond yields, exchange rates and share prices, none of which are controlled by the Fed. The Goldman Sachs Financial Conditions Index, which incorporates these three factors along with short-term rates, suggests that overall monetary conditions are roughly the same today as they were when the Fed started to raise rates in June 2004. Although bond yields have edged up during the past two months, they are still lower than before the Fed started to tighten—indeed, they are unusually low in real terms—offsetting the rise in short-term rates.

Long-term bond yields have more influence on America's economy than do short-term rates, not least because most Americans still have fixed-rate mortgages. Low yields are thus frustrating the Fed's effort to tighten monetary conditions. Despite the rise in short-term rates over the past year, America's GDP growth is well above trend, and although consumer prices remain tame for now, slowing productivity and a strengthening labour market could push up inflation. But the economy is unlikely to slow until the housing market cools, and that is unlikely to happen without higher bond yields.

Push harder

As a result of the international integration of capital markets, bond yields are increasingly set by global economic developments rather than just by domestic factors. But while it is convenient to blame the global bond market for America's lax financial conditions, some of the blame also lies in Washington. Ten increases in short-term interest rates may sound tough. However, the truth is that American rates are still unusually low in real terms and well below the 6% pace of nominal GDP growth. The Fed still needs to tighten financial conditions in order to put the economy on a sustainable course. If bond yields remain low, the Fed will have to raise rates by more than otherwise. Most economists interpret that as implying that the Fed will continue to lift rates by a quarter-point at each meeting, but to keep going for longer. Yet if the Fed really wants to withdraw the current monetary stimulus, it might be better to opt for a half-point rise to get there faster.

The most popular explanation for low bond yields is global excess saving. However, excessively loose

monetary conditions worldwide may also be a factor (see article). Global excess liquidity (for which the Fed is partly responsible) is inflating the prices of not just shares and houses, but also of bonds. It may be time to call out the lifeboat.

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Japan's general election

The bravery of Junichiro Koizumi

Aug 11th 2005
From The Economist print edition

It deserves, for Japan's sake, to be rewarded

KABUKI plays, at least to the untutored and no doubt philistine eye, seem mostly to have the same plot: a socially impossible relationship that ends with a double love suicide. The four years during which Junichiro Koizumi has been Japan's prime minister have followed a similar pattern. For a fairly market-friendly reformer to have led the conservative Liberal Democratic Party (LDP) which has ruled Japan for all but ten months of the past 50 years, which built its power on big government and which bears much of the blame for the economic mess Japan has been in since 1990, was always a rather improbable affair. Accordingly, it has been accompanied by bouts of wailing and leaping through the air, as well as by magical machinations behind the scenes. On August 8th, however, when he lost a crucial vote in the parliament's upper house, Mr Koizumi decided to jump to the final act by calling a general election for the main, lower house on September 11th, two years ahead of schedule (see article). But in his play there is a twist: his is a double hate suicide.

It may not in fact turn out as a double suicide, but that is certainly what Mr Koizumi is risking. By challenging the old guard in his party and by ejecting the 37 LDP parliamentarians who voted in the lower house against his flagship scheme, the privatisation of Japan Post, setting the stage for its upper house defeat, he is deliberately splitting his own party and thereby risks losing power to the main opposition, the Democratic Party of Japan (DPJ). By threatening dissolution if he did not get his postal bills through, Mr Koizumi must have thought that his LDP opponents would back down for fear of bringing on their own demise. But they didn't. In Japanese politics, as opposed to Kabuki, this is a rare and unfamiliar drama. Yet it is extremely welcome.

Let reform be the winner

It is possible that Mr Koizumi will win a remarkable victory in the election and lead a new phase of reform himself, at the head of a purged LDP. But even if this double hate suicide does end up being fatal both for him and the LDP, the outcome is likely still to be a good one for Japan and much to Mr Koizumi's credit. For the debate between him and the alternative government, the DPJ, is no longer about whether to reform Japan in a more market-friendly direction but how. Even if the DPJ wins, Mr Koizumi will have succeeded in injecting reform right into the bloodstream of Japanese politics.

He has had a frustrating time trying to do so, and those who sympathise with his goals—which includes

The Economist—have often found his prime ministership frustrating too. The Japan he took up the leadership of in 2001 had lain in the doldrums for 11 years, never having had the crisis that might have forced it into reform, but also never achieving a gradual, consistent, consensual reform either, thanks to the power of special-interest groups to obstruct change. Banks were burdened with a huge pile of dud loans, the public-sector deficit was nearing 8% of GDP, companies had too much production capacity and prices were falling in a debilitating deflation. Yet the very solution that had been adopted for Japan's macroeconomic problem after its stock- and property markets crashed in 1990, a big expansion of public-works spending, ended up making reform harder. It provided a luscious flow of cash for LDP politicians to use to buy votes and to enrich their supporters, especially in the construction industry, and gave the bureaucracy even more power to direct the economy, not less.

Faced with this situation, Mr Koizumi was very much the man for the moment. For decades, he had been obsessed with breaking up or privatising Japan's postal system, which sounds a strange obsession but actually lies at the heart of the country's financial and political distortions. For delivering mail is the least of what it does: it is also the world's biggest bank by some measures, with deposits and life-insurance policies worth some ¥331 trillion ($3 trillion). These are offered to the public at subsidised rates, thus undercutting commercial banks and insurers, and then shovelled to the government to finance a vast “second budget” of subsidised loans and public-works schemes. If you could break that up, and with it the corrupt system of allocating public money for building bridges and roads, you could really set Japan on a better course.

But he couldn't. The opposition from his own party, from the construction industry and postal workers, and from much of the bureaucracy, seemed too great. His effort to break up and privatise the road-building agency, the Japan Public Highway Corporation, had to be heavily watered down. Finally, four years later, he tried to break the postal system into four companies and privatise them, albeit in a slow process due to last until 2017. And this week he failed.

Yet, though Mr Koizumi's few big, headline-grabbing efforts have foundered, leading him to this gamble, he has actually achieved quite a lot in quieter ways. He turned the country's bank regulator from a patsy of the banks (another interest group) into something more powerful and independent. He slashed the flow of money in public works: public investment has fallen from 8% of GDP in the 1990s to 5% now. So although the structure hasn't yet changed, the financial parameters have. And he has strengthened the role and powers of the prime minister, both within government and within his party, making it easier in future for reform to be directed from the centre. Meanwhile, time, corporate restructuring and exports to China have been great healers for the economy, putting the country into stronger shape to accept reform too. All that is without even mentioning his changes to foreign policy, sending troops to Iraq and generally being more assertive.

If Mr Koizumi can win an electoral endorsement for the shrinking of government and the liberalisation of the economy, then that will be all to the good. But if the public decides instead that the LDP as a whole deserves to be kicked out at last, then the DPJ too shows every sign of favouring liberalisation—despite its tactical opposition to the postal bills. It is more tragedy than comedy that it has taken so long for Japan's politics and economic policies to get shaken up. But now there is every prospect of a heart-warming ending.

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Israel's settlers

Waiting for a miracle

Aug 11th 2005 | THE GUSH KATIF SETTLEMENTS
From The Economist print edition

AP

The row over Israel's biggest evacuation of settlers in over two decades presages a growing clash over what makes the Jewish state Jewish

IT IS the last Sabbath eve in July, a night of stillness and velvet warmth after the heat of the day. The villa-lined, traffic-free streets of Neve Dekalim are dotted with people strolling home from family dinners or chatting softly to neighbours. Then a loudspeaker breaks the calm. “Residents, good evening and good Sabbath. Please go into protected buildings immediately.”

The people respond to the warning as they did to the dull crack of the mortar shell that fell an hour or so earlier. They pay not the slightest attention.

Miracles in Neve Dekalim are a part of everyday life. According to the settlers' count, some 6,000 mortars and Qassam rockets fired from the Palestinian towns in Gaza have fallen on them since the second *intifada* erupted five years ago—nearly one for every settler. Yet only one settler has been killed. Clumsy weapons, a statistician might say, and a thinly spread population, in detached houses and large gardens. But in the words of Ruth Cohen, of nearby Ganei Tal, “Every time a mortar comes over, God bats it away with a *matka*.”

The belief that the Almighty amuses Himself by playing Israel's national beach sport with explosive shells is also why many have not even started packing, deciding where to live or applying for compensation. On August 15th the army is due to start evicting the Gaza settlers, as well as those in four isolated West Bank communities. But some will wait and see. God may mean them to leave Gaza—temporarily. If not, He will somehow stop it from happening.

Most Israelis cannot grasp this thinking. Nor can they grasp why anyone would live in a hot, sandy, bombarded enclave, surrounded by barbed wire and watchtowers, much less put their children in such danger. It must be out of religious fanaticism, or else a twisted urge to make life hell for the 1.3m Palestinians squeezed into the rest of the Gaza strip.

“Look beyond the ideology,” urges Gideon Aran, a sociologist at the Hebrew University in Jerusalem. The answer “quality of life” seems a bad joke, but everybody in Gush Katif, religious (the majority) and secular, gives it. It is not just the big houses and quiet streets. Insulated from the rest of Israel as much as from the Palestinians, the place evokes an older, more innocent time. Doors are left unlocked. Parents do not worry where their children are at night. Many inhabitants, former residents of poor, charmless towns, also find a sense of community, of building something new. The phrase “Garden of

Eden" is even heard.

But whereas Adam and Eve knew why they must leave, the settlers cannot understand their original sin. The government encouraged them to move there—some after being evacuated from Yamit, the settlement strip at the north of the Sinai, when Israel gave it back to Egypt in 1982. Relations with the Palestinians used to be just great. Even the more secular settlers invoke historical ties to the land going back to biblical times. They thought they were broadening the borders of the state. Instead they have found themselves on a sort of spacewalk outside it, kept alive by a barrage of protective technologies that ordinary Israelis are sick of paying for, and by miracles, which they don't believe in.

The fall from grace will be a hard one. To leave is not just to throw away the years or decades invested in building houses, businesses, farms and communities and to search, perhaps fruitlessly, for new jobs. It is to return to an Israel that has grown alien: to being, as Mr Aran puts it, "rank-and-file citizens in a stinking political and civic reality". And for what? Like many in Israel itself, they are sceptical that the "disengagement" will bring any benefits; rather, they fear that Palestinian extremists will take it as a sign that terrorism works.

Nearly half a million Israelis live on Palestinian land occupied in the 1967 war. The vast majority are in settlements not far over the pre-war boundary (the Green Line), where living standards are higher or prices cheaper; they do not even consider themselves settlers, though most international bodies do. The "ideological" ones in the more distant colonies, on the far side of Israel's "separation barrier", number fewer than 100,000. In Gaza, 8,000 or so are being evacuated. And Gaza matters far less economically, strategically and biblically than the West Bank.

Yet much more is at stake than Gaza itself. The settler movement as a whole sees disengagement as the thin edge of a wedge that will eventually lever Israel out of the West Bank and parts of Jerusalem as well. The argument over Gaza has also become a bitter trial of strength between Israel's so-called "mainstream", the mostly secular Jews who say they would gladly give up land for peace, and the national-religious settler movement. That movement has grown ever more powerful since the war of 1967, and seemed until Ariel Sharon's "betrayal" to have imposed an unbreakable armlock on the state itself. The outcome of this struggle may determine whether Israel is ever capable of making peace.

Hastening the Messiah

The existence of religious Zionism, let alone its present strength, is an oddity, since the original Zionism was areligious, even counter-religious. Its founders, secular Jews inspired by the nation-state enthusiasm sweeping 19th-century Europe, saw emigration to Palestine as a way to escape not just the squalor and persecution, but also the stifling insularity and religious orthodoxy of *shtetl* life. It took the first chief rabbi of British Mandate Palestine, Abraham HaCohen Kook, to argue that a Jewish return to the land could hasten the coming of the Messiah and the final redemption.

At first, says Yedidia Stern, a scholar at the Israel Democracy Institute, this was an underground

movement. But Israel's lightning-swift capture of territory in 1967 from Syria, Jordan and Egypt seemed to prove, to Kook's followers, that the Jewish state was indeed part of the messianic plan. Suddenly the promise in the book of Deuteronomy had a new ring: “You will dispossess nations larger and stronger than you. Every place where you set your foot will be yours.”

The almost-defeat of the 1973 war only strengthened the religious Zionists' resolve. They set up a movement, Gush Emunim, “the block of the faithful”, which took on settlement in the territories as a holy task. And religious Zionism became the mainstream ideology for observant Israeli—or “national-religious”—Jews.

They had willing allies. The secular Zionism of those days was no less messianic, says Mr Stern, with settling land as one of its key values. The Labour Party produced a modest settlement plan, mostly for a strategic presence to secure the new eastern border. After the right-wing Likud defeated Labour in 1977, Mr Sharon, the new minister of agriculture, was more ambitious. His plan added a series of industrial towns along the hills near the Green Line, and a strategic ring of Jewish suburbs around occupied East Jerusalem. He promised his fellow ministers 2m Jews in the occupied territories by the end of the century. The calculation, say Akiva Eldar, a journalist, and Idith Zertal, a historian, in “Lords of the Land”, a recent book on the settlements, was to make the settlements command the territory and overlook it. “The unconcealed goal”, they add, “was to thwart any future possibility of setting up a viable Palestinian state with reasonable territorial contiguity.”

But to avoid international criticism that settlement in occupied territory is illegal, it was often done in roundabout ways. Young zealots would start, for instance, by taking on construction work at an army base in the territories. At first they would commute. Then they would try to set up a camp. Often they would be thrown out, and try again. Eventually, thanks to a sympathetic or neglectful official, they would be allowed to stay “temporarily”. A generator would follow, then families, permanent homes—“facts on the ground”, in the phrase that has become a bitter national joke—and only then, official permission.

As the settlers' influence grew, the subterfuges multiplied. A 1983 state auditor's report complained, in vain, that most building in the territories was without local or regional planning, and that settlers themselves were essentially deciding budgets. To this day, “settlement outposts” continue to crop up in seeming contradiction to official policy, thanks to friends in the right places.

All the while, however, the breach between the religious and secular was growing. Israel's left and even much of its right has lost faith in “Greater Israel” thanks to military setbacks, Palestinian *intifadas*, and, not least, demographics. The Palestinians between the Mediterranean and the Jordan river will soon outnumber Jews. Keeping the occupied land will force on Israel the impossible choice of being either an apartheid state, or a binational one with Jews as a minority.

Today many mainstream Israelis, both secular and religious, resent the settlers for the state benefits they have enjoyed, for exacerbating the conflict with the Palestinians—and not least for expropriating the colour orange, as in Ukraine, for their rebellion, thus forcing untold numbers of summer outfits to stay in closets. Most would happily give up the farther-flung settlements so that Israel can be both Jewish and a democracy. So would even many religious Zionists, now about a fifth of Israel's population, says Otniel Schneller, a former chairman of the Yesha Council, the umbrella group of settlement mayors.

Sharon's betrayal

It was in this atmosphere, with the second *intifada* already raging, that Mr Sharon was elected prime minister in 2001. His opponent, Labour's Amram Mitzna, had promised to disengage from Gaza. Mr Sharon promised not to. But in December 2003 he announced a plan to do so.

Why? The kindest theory is that he simply, suddenly, grasped the demographic reality. (Israel will, in any case, reserve the right to send the army back in to Gaza if necessary; in effect, it will remain occupied.) But the move is not inconsistent for Mr Sharon, argues Mr Eldar, because “Gaza was never part of his vision.” Withdrawing might even strengthen Israel's case for keeping control of the West Bank if, as looks likely, the Palestinian Authority (PA) turns out to have no authority in Gaza. Some, in fact, think that that was Mr Sharon's calculation.

Yet the plan has alienated not just the Gaza settlers, but a large part of the religious-Zionist mainstream that could have been supportive. Partly it is because Mr Sharon, the settlers' godfather, is the one pulling them out. His heavy-handed tactics did not help. He ignored a vote in his own Likud party against the plan; fired ministers who refused to back it; rejected calls to hold a national referendum on

it (opinion polls showed a majority favouring the pull-out, but settlers believe that polls undercount the religious vote and that a referendum campaign would have swung the balance); and finally scheduled it during the three weeks leading up to the fast-day of Tisha B'Av, when religious Jews do not move house. (It was later shifted.)

Moreover, the preparation was hasty and slapdash. The government started surveying new sites and building temporary homes just a few months ago. (Yamit's residents had three years to get ready; they moved to farms that they had already started planting.) And the benefits are dubious. There is no peace deal, as there was with the Sinai withdrawal. Qassam- and mortar-launchers will now be able to come closer to the Gaza-strip border and reach more targets in Israel.

A widening schism

The withdrawal itself may pass off more smoothly than expected. Aside from a few extremists, the settlers will leave their homes sadly but without resistance. But it has turned into a much bigger conflict, widening existing splits in the political parties, in the religious-Zionist movement and between religious and secular Israelis.

Mr Sharon's adoption of the withdrawal plan emasculated the Labour Party, which was forced to support its arch-enemy. But it split the Likud. A third of the party's members in the Knesset, Israel's parliament, opposed it; this week Binyamin Netanyahu, the finance minister, resigned, saying he could not back it. His is an opportunistic gamble. If the withdrawal is seen as a failure—if it leads, for instance, to more terrorism from Gaza—he will be in a stronger position to challenge Mr Sharon for the Likud leadership ahead of general elections, which must be held by November 2006.

Among the religious, people are becoming both more moderate and more radical, says Netty Kupfer, a co-founder of Realistic Religious Zionism, a group that is trying to find common ground. A minority of hardliners are taking the state's disengagement from Gaza as a cue to disengage from the state. One *yeshiva* in Gush Katif refused to celebrate Israeli independence day this year. At the Neve Dekalim synagogue, a man keeps his mouth shut during the prayer for the state of Israel and is berated by his neighbour: “Sing! You want to go back to the diaspora?”

Others, more optimistically, have begun to see the expulsion as a sign from God to reconnect with Israel as a whole, by setting up the nuclei of religious neighbourhoods in the cities they had shunned. “To settle in hearts instead of on hilltops,” in the words of Rabbi Yoel Bin-Nun, a Gush Emunim founder who laments that the movement didn't do enough of it earlier.

EPA

This says it's ours

But mainstream religious Zionism has also come out of the conflict emboldened. It is a movement without a political wing: the National Religious Party in the Knesset is tiny, and other religious parties were happy to back the disengagement in return for concessions on matters such as religious education. But it has shown that it can mobilise people in a way the left can only dream of. A “blue” pro-disengagement campaign has fizzled miserably; orange ribbons outnumber blue on Israel's cars by at least ten to one.

And while there were protesters of all ages, the young predominated. A poll in the *Yediot Ahronot* newspaper at the end of July found that while most Israelis still backed the disengagement, most under-35s were against. Part of a generation, in other words, has been politicised by the Gaza

pull-out—and it is right-wing. Comparisons are drawn with the 1968 protests in Europe and the Americas, which marked a generation of future leaders. “Except that there, it was an anarchic protest against state authority,” says Mr Stern. “Here they are challenging state authority with a different kind of Authority.”

All this further drives in the wedge between secular and religious Israeli Jews. “The debate is about what the Jewish component of the state of Israel means,” says Rabbi Michael Melchior, a government minister and founder of a moderate religious party, Meimad. “The settlers have succeeded in making [the withdrawal] a story of Judaism versus emptiness. They have turned it into a *Kulturkampf*.”

That conflict will find expression in many ways in the years to come. The most obvious is over future withdrawals. The West Bank barrier that Israel is building, on “security” grounds, to enclose the main settlement blocks is clearly meant to complete anannexation of the land they are on. Most Israelis support keeping them. (So does George Bush, who has spoken of recognising “facts on the ground”.) And most would give up the small, distant settlements in the Jordan Valley if there was something to show in return.

It is the ideological settlements just beyond the barrier that will cause the most conflict. A majority might support abandoning them for a true peace deal between Israel and the PA. But that looks a long way off. Mr Sharon is in no hurry to reach one. And another unilateral withdrawal, with no obvious benefits attached, may be impossible. If the settlers' resistance movement remains strong, the claim that the Gaza pull-out has set a precedent for future withdrawals looks extremely shaky.

Withdrawals aside, says Mr Kupfer, the next crisis could be over other aspects of the state's Jewish character. Should there be civil marriages, rather than just rabbinical ones? Should there be public transport on the Sabbath? Should the state continue to support Jewish religious education? Over the years, pressure from the left has eroded such vestiges of religious interference in civil affairs.

Now the tide could start moving back. Ironically, even though the settlers lost Gaza, it is the right, which should have suffered most from the disengagement, that has been re-energised by the battle. Whatever happens after August 15th, Israel's own clash of civilisations is only just getting into its stride.

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Terrorism and civil liberties

Watch your mouth

Aug 11th 2005
From The Economist print edition

Tony Blair thinks that European human-rights laws prevent Britain from dealing with supporters of terrorism. But the real obstacles lie closer to home

WHAT makes a suicide-bomber? Long before the attacks in London, Britain's security services had a clear pattern in their minds. A man who may drink beer, play football, chase girls and lead a life that is indistinguishable from those of most other young Brits starts looking around for something less ordinary. At that point, he comes under the influence of a charismatic imam, who rails against the ill-treatment of Muslims around the world and suggests a straightforward route to self-fulfilment. He may eventually board a plane to Israel or a train to London, with the intention of killing as many civilians as possible.

Trying to prevent rebellious impulses from taking hold is a difficult thing for a parent to do, let alone a government. So Labour is looking instead at clamping down on the people who inspire terrorists. Many of these people, it thinks, are foreign-born, and therefore the state ought to be able to deal with them, without the liberties that British citizens enjoy getting in the way. That was the impulse behind a plan launched by Charles Clarke, the home secretary, to define what counts as unacceptable behaviour by Muslims in Britain. It was also behind the 12-point plan that Tony Blair announced on August 5th, while his home secretary was on holiday, before he too headed for the beach.

Mr Blair's agenda is wide-ranging and vague. It includes speeding up the deportation of foreign-born radicals, extending a proposed ban on glorifying terrorism to cover people who justify or glorify terrorism anywhere in the world, holding pre-trial hearings to allow sensitive evidence to be admitted (these have already been dubbed “secret courts”), banning some Islamist organisations from Britain and closing troublesome places of worship.

That was more than enough to frighten libertarians. “Just having undergraduate debates about whether it is ever right to take up arms could get you into this,” reckons Shami Chakrabati, director of Liberty, a pressure group. But then the attorney-general raised the temperature further, by letting it be known that radical imams might be charged with treason, an ancient crime in English law that dates back to an era when having sex with the king's consort was a capital offence.

Part of this is politicking. “Everything the prime minister said will go down well in Conservative associations”, Edward Garnier, the Conservative shadow home affairs minister, notes gloomily. The treason idea was quickly scotched, though not before it had inspired some headlines. But Mr Blair's insistence that “the rules of the game are changing”, plus a nagging suspicion that Britain's legal system might be less well equipped to deal with Islamic extremism than those of other European countries, has left the government looking for ways to make Britain a bit more like France (see article). According to Mr Blair, the first step in that process is to find a way around the 1998 Human Rights Act.

That's odd, because the other members of the Council of Europe are also bound by the European Convention on Human Rights (which British civil servants played a big part in drafting). Though Mr Blair says that Article 3, which prohibits torture, makes it difficult to deport undesirables to countries where their toenails might be pulled out, this has not prevented other signatories to the convention from doing so. So what is Britain's problem?

First, though the convention is the same everywhere, the adversarial legal system means that it works differently in Britain. Defendants typically have the right to appeal at several stages of the legal process. That makes appeals against extradition protracted and expensive. In 2001, it took an average of eight months to extradite someone to Britain, but 18 months to send someone the other way. Contested hearings cost around £125,000 ($223,000). An attempt two years ago to streamline the process has not altered its fundamentally fractious nature. In France, by contrast, deporting suspects to countries with patchy human-rights records causes little fuss. Rights of appeal are more restricted and deportees may not be able to appeal until after they have left the country, by which time it might be too late. “Often

you send a fellow back to Algeria and that's the last you hear of him," says Clive Walker, who studies terrorism laws at Leeds University.

Second, Britain has a long tradition of sheltering firebrands, which is reflected in the law. Victorian London was an excellent place for foreign radicals to set up shop—whether they were scholarly types like Karl Marx, who plotted the overthrow of capitalism from the reading room of the British Museum, or militants like Johann Most, a German anarchist who was allowed to wander the streets despite penning a guide called "The Science of Revolutionary Warfare". Ancient laws on free speech, a light touch from the censor and a lack of legal distinctions between citizens and non-citizens have appealed to African National Congress supporters and Islamist radicals alike. If the government really wanted to overturn this tradition, it would need extensive legislation.

A more straightforward option is to get agreements from foreign countries not to harm anyone who is extradited from Britain. It already has one such agreement with Jordan, and is seeking similar undertakings from nine other countries. On August 11th, police arrested ten foreign nationals in south-east England and the Midlands, with a view to deporting them. It will provide the first test of how judges respond to Mr Blair's hectoring.

None of this helps much where the culprits are British-born, however. For them, the government proposes to use more control orders—a new legal device that deprives people of some liberties without actually locking them up. Mr Blair also said that the government would look at stripping naturalised Brits of their citizenship if they support terrorists. In practice that's difficult: unless someone has dual nationality, revoking their citizenship means making them stateless.

Some have suggested that the flurry of announcements, coupled with a lack of detail on how they might work, is really aimed at scaring the extremists away. If so, it might be working. Omar Bakri Mohammed, a Syrian-born imam who could be caught out by the new laws, has left Britain to visit his mother. However, reports that he had been detained in Lebanon may deter other firebrands from doing the same.

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Religious schools

Abode of Islam

Aug 11th 2005
From The Economist print edition

Are Muslim schools standing in the way of integration?

Get article background

SINCE the London bombings on July 7th, fears have been growing that Britain is not only allowing, but actually facilitating, the creation of a radicalised Muslim community in its midst. Politicians, including some Labour ones, have attacked multicultural policies and demanded that Muslims integrate more fully. Among the targets of criticism are Muslim schools.

Around 25,000 of the more than 500,000 Muslim children in Britain are educated in the country's 100-odd Muslim schools. The five that have joined the state sector since Labour came to power in 1997 are wildly popular: the first to do so, Islamia Primary School in London, admits 30 children a year, and has another 2,500 on its waiting list.

The others are independent, which gives them more freedom to teach the subjects they want. To secular eyes, the results can be odd. Alongside subjects from the national curriculum, one large, highly regarded private girls' school offers principles of faith, Islamic jurisprudence, Koranic recitation, Islamic history and the study of the life of the prophet Muhammad—as well as Asian cooking, healthy eating and dressmaking.

It is likely that the few Muslim state schools will soon be joined by others. The Association of Muslim Schools UK (AMSUK) says that most of its 108 independent member schools would like to move into the state sector. That would mean they would have to teach the national curriculum and satisfy the government's education watchdog that they offer a fully rounded education. They should also, according to government recommendations, reserve at least 10% of their places for non-Muslim children, although those already in the state sector say that they don't get enough applications from such children to fill this quota.

The transformation will not happen quickly. Joining the state sector requires schools to prove that their education and facilities are up to scratch. This is difficult for schools that tend to be run on a shoestring: fees are far lower at Muslim schools than elsewhere in the independent sector, with some day schools charging as little as £1,000 ($1,800), and even some boarding schools charging less than £3,000 a year.

But the government is keen to nudge things along because it feels that the way to keep Muslim schools moderate is to bring them into the heavily-regulated state sector. Even if they stay put, however, they will be watched more closely. Since 2003, independent schools have had to submit to regular government-approved inspection, and from September 2005 they must be registered with the state. Although they won't have to teach the national curriculum, they will have to show that they provide reasonable standards of teaching and accommodation, teach mainly in the English language and ensure that students gain a detailed understanding of British laws, customs and culture.

AMSUK says that most of its members will meet the September deadline. A handful of seminaries won't, however. These train imams, and devote most of their syllabus to Islamic studies. About 3,000 children aged 12 and up attend seminaries in Britain, most of them large and professionally run. A few small ones, however, are unlikely to meet the required standards, and will be forced to close.

The charge that Muslim schools entrench segregation in British cities is partly true. But the country's roughly 7,000 Christian state schools can create equally strong barriers to integration. In many places with large Muslim populations, most non-Muslim children go to church schools, leaving secular schools to become Muslim by default.

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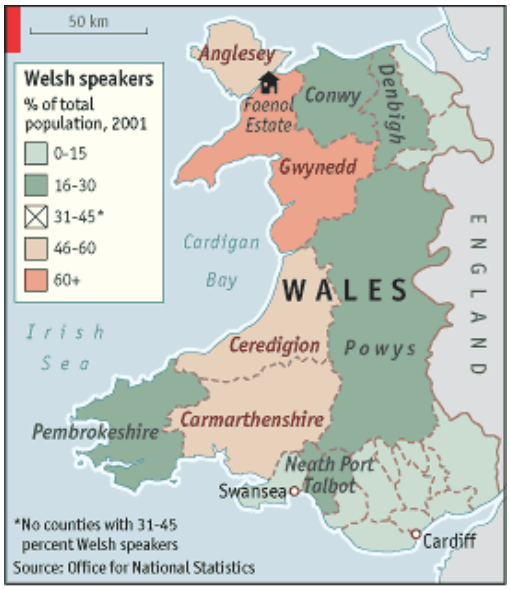
Welsh

From mother tongue to meal ticket

Aug 11th 2005 | CARDIFF AND FAENOL
From The Economist print edition

Why the Welsh language is making a comeback



SCARCELY a word of English was uttered last week in Faenol, a grand estate that hosted the Eisteddfod, a sort of nationalistic arts festival for Wales. Nor is English the local language of choice. In this region, Welsh takes precedence on road signs—and the English words are often illegible, thanks to the patriotic application of spray paint. In the county of Gwynedd as a whole, 70% of people can speak Welsh. Walk into a shop here, and the conversation is likely to begin: “Ga i helpu?”

Given the nearness of England, an infamous linguistic coloniser, the mere survival of such an ancient language is remarkable. Odder still, Welsh is holding steady. Between 1991 and 2001, the share of the population who claimed to be able to speak the language actually went up from 19% to 21%—the first increase in over a century. And the proportion of Welsh-speakers is likely to increase further, since teenagers are much more likely to be able to speak the language than their parents.

That ought to be a source of pride in a country where identity is closely tied to the ancestral tongue. While Scottish nationalists demand political independence, the Welsh just want everyone to speak the lingo. Since 1993, public agencies have been obliged to provide a bilingual service, even in areas where few people understand Welsh. Court cases can be heard entirely in the language, if the plaintiff or the defendant chooses. Midwives even encourage new parents to speak the tongue to their babies.

Yet Welsh-language campaigners are in a dismal mood. Aran Jones of Cymuned (Community) believes the language is in a much worse state than national statistics suggest. In the hilly north and west of Wales, where the native language is strongest, the Welsh-speaking population is being diluted by migration (which Mr Jones calls “colonisation”) from England. Children may be familiar with Welsh, but only in the sense that English schoolchildren are familiar with French—as an academic discipline, not as a natural tongue.

Welsh is, indeed, slowly dying in the heartlands. Between 1991 and 2001, Welsh speakers declined in number in the five mostly rural counties where they had been most common. As a rule of thumb, say linguists, a minority language will die out if it is spoken by fewer than 70% of the population.

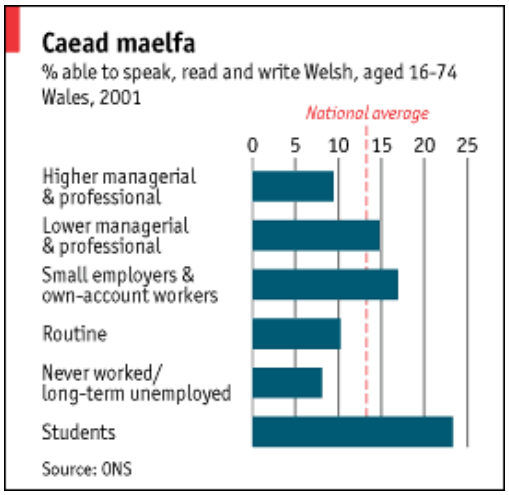
Ominously, the number of wards where that density was achieved fell from 87 to 58 during the 1990s.

Nationalists are divided over what to do. The extreme 1960s and 1970s response, which consisted of blowing up pipelines and burning holiday cottages owned by Anglophones, is out of style. The Welsh Language Society, a pressure group that has seen many of its demands incorporated into law, wants restrictions on house-building in Welsh-speaking areas and a language act that would require businesses to deal with customers in their preferred language. One of its members went on hunger strike during the Eisteddfod, just to show it was serious. Cymuned believes still more drastic measures are needed. It wants independence for the Welsh-speaking heartlands.

The battle for the heartlands is bound to end in defeat. But Welsh is growing in places where it was virtually unknown a few decades ago. In Cardiff, where the signs are bilingual (but, significantly, English takes precedence over Welsh), the proportion of people who can speak the language has increased from 5.8% to 10.9% in the past two decades. More than a tenth of the population of Wales lives in the city. Welsh is also growing rapidly in the former industrial and coalmining area of south Wales known as the Valleys.

That may partly be because these are the ugliest bits of Wales, so English settlers tend to steer clear of them. But the main reason is probably the growth of Welsh schooling since the 1960s. There are now 448 primary schools and 54 secondary schools that teach mostly or entirely in Welsh, many of them in the south-east. They tend to be good schools, so many middle-class parents who do not speak Welsh patronise them.

As a result, says Colin Williams, a Cardiff University linguist, the schoolroom is replacing the home as the main pillar of the language. And pupils pick up more than Welsh. Because the demanding parents who send their children to Welsh-language schools tend to have demanding children, the schools are nurturing a new generation of articulate nationalists.



Another reason for the growth of Welsh has to do with the job market. Many of the best paid, most stable and most interesting jobs in Wales demand knowledge of the language—or are thought to demand it, which is just as important. Thanks to the language laws, the country's swollen public sector is hungry for bilinguals; so are the burgeoning government-supported Welsh media. According to the 2001 census, 20% of people employed by culture, media or sporting outfits could speak, read and write Welsh, compared with just over 13% of all people aged 16-74. That, in turn, encourages politicians and other public figures to learn the language. Lisa Francis, a Conservative member of the Welsh Assembly, says she has given more interviews in Welsh than in her native tongue. All but two of her ten colleagues speak Welsh or are learning it.

Welsh-speakers tend to be middle managers or small-business owners (see chart). They are less likely to be found in the highest ranks of business and the professions, but they are also much less likely to be unemployed than monoglot English speakers. High demand means that they earn more, too. A recent study by Andrew Henley of Swansea University found that, after controlling for residence and education, Welsh speakers earned 6-8% more than the competition. Another study, for the Welsh Assembly, estimated the earnings premium at more than 10%.

There is a message here for other linguistic nationalists, from the Québécois to the Basques. Forget bombings and hunger strikes: to ensure the survival of a language, create a closed shop.

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Interest rates

Cold shower

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The Bank dampens hopes of interest-rate cuts

Get article background

WHEN the Bank of England cut the base rate last week from 4.75% to 4.5%, the markets were not surprised. Since then, the City has been wondering how far rates were likely to fall. The Bank's Monetary Policy Committee (MPC) gave a signal in its quarterly *Inflation Report* on August 10th: not much further, it implied.

In the run-up to the MPC's meeting, the markets were expecting the base rate to fall to around 4% by early next year. But if this were to happen, the Bank forecasts that consumer-price inflation would be above the government's 2% target in two years' time—the period it takes for interest-rate changes to work their way fully through to inflation—and rising (see chart).

By contrast, another forecast by the Bank shows that if rates were held over the next two years at 4.5%, inflation would be on target in mid-2007. So on the face of it, the MPC appears to be signalling that the first cut will also be the last cut.

The Bank's main projection is that the economic slowdown is nearly over. In the past 12 months, growth has decelerated appreciably. GDP increased by 1.7% in the year to the second quarter of 2005, the slowest for 12 years. The Bank thinks that growth will remain sluggish for the rest of the year but that the economy will then regain speed. By the end of 2006, GDP will be growing at an above-trend 3% a year.

This expectation of an upturn has several sources. For one thing, the MPC is quite upbeat about the growth prospects for the world economy and now forecasts a gentle recovery in the euro area, Britain's principal market for exports. For another, it thinks that demand will be buoyed by the rise in share prices and the fall in the exchange rate over the past three months. Furthermore, the Bank now expects business investment, which has been surprisingly weak, to pick up a bit.

As important, the MPC is sticking to its line that the link between the housing market and consumer spending has become considerably weaker than in the past. As a result, consumption should take less of

a knock from the downturn in the housing market. Household spending juddered to a virtual halt in the first quarter, growing by just 0.1%. However, the Bank thinks this will prove a temporary setback and is forecasting a revival in consumption, although it will grow below trend.

Even so, there are risks to the main growth forecast and the Bank accepts that they are on the downside. In particular, it worries that the short-term outlook for consumer spending may prove more disappointing than its central projection. If the downside risk to growth materialises, inflation would be correspondingly lower.

With consumer debt at a record high and the housing market fragile, the downside risk to household consumption could be higher than the Bank is contemplating. That risk is all the greater since the labour market is now softening. Furthermore, companies may remain tight-fisted in their investment plans.

Since the Bank itself acknowledges a downside risk to activity and inflation, the most plausible interpretation of its new forecasts is that it will lower rates once again, to 4.25%. But that shallow rate-cutting scenario will not long survive a new batch of evidence that the economy is set to weaken further.

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Exams

Devaluation

Aug 11th 2005
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Evidence that A-levels are worth less than they used to be

PA

Quantity not quality

Get article background

A-LEVELS are often called the “gold standard” of British education. But each year, when students are awarded record grades (as will no doubt happen next week, when this year's results come out), critics claim that their value is being eroded.

It is hard to judge whether that's true, since changing syllabuses and subjects make it difficult to track standards over time, and the growth in numbers of students taking A-levels and going to university makes it useless to look at changes in purchasing power. However, the Universities and Colleges Admissions Service (UCAS), which processes applications for many British undergraduate courses, has just provided some information, based on the exchange rate between A-levels and the Irish Leaving Certificate (ILC), which suggests that the value of A-levels is indeed declining.

British institutions have long regarded an ILC as worth half an A-level. This works neatly: they normally look for three A-levels, while universities in Ireland typically look for six ILCs.

But in formalising the worth of an ILC, UCAS has re-valued the Irish currency. From 2006, an ILC should be regarded as equivalent to two-thirds of an A-level. Arguably, the adjustment was long overdue. Either young Britons are massively cleverer than young Irish people, or it is easier to do well in A-levels than in ILCs: more than 20% of all results are As and 9% of all students taking A-levels get three or more As. By comparison, fewer than 1% of all ILC-takers get six or more As.

In future, most British universities will regard Irish students' qualifications more highly than before. Some Irish institutions have downgraded A-levels accordingly. From next year Trinity College, Dublin

will be looking for four A-levels from British applicants, rather than three. Students with only three A-levels must resign themselves to missing out on the most competitive courses, such as medicine and law.

Not many British students take degrees in the Irish Republic, so the immediate impact of the devaluation will be limited. But, even if you never travel abroad, when your country's currency is devalued you will eventually feel it.

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Alternative fuels

Greener than thou

Aug 11th 2005
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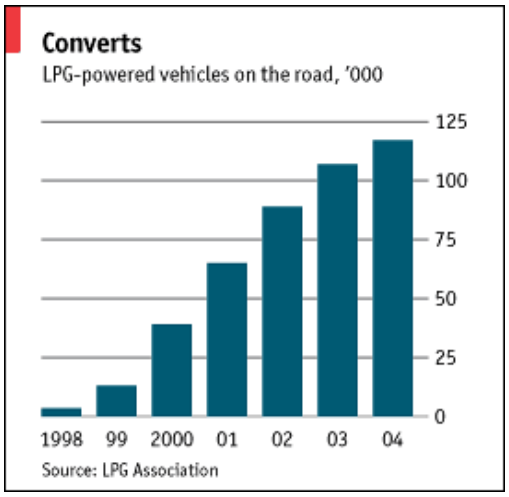
Liquefied petroleum gas is becoming more popular among drivers



MOTORISTS in Britain think themselves beleaguered by a combination of sneaky speed cameras, car-hating greens and, worst of all, exorbitant petrol prices. Last week these hit 90p per litre, the highest nominal level ever (but about the same, in real terms, as in 2000, when fuel price protesters jammed the roads).

Happily for irritated drivers, there are alternatives to pricey petrol and diesel. The most widespread is Autogas, a form of liquefied petroleum gas (LPG) designed for use in specially-converted cars. Taxes on LPG are low, and at around 39p per litre it offers much cheaper motoring than conventional fuels, although fuel efficiency is slightly lower. Environmentalists are keen on LPG, too, since it produces fewer damaging emissions.

The number of LPG-powered cars on the roads is growing briskly, albeit from a low base (see chart). Yet compared with other countries, Britain lags. Italy, Poland and South Korea have over a million each.

Partly that's because of the early adopter problem: consumers will have their cars converted only if fuel is easily available, but companies will be willing to sell it only when there are enough drivers to make it profitable. Currently, 1,276 garages, about 10% of the total, sell LPG. Another problem is economic. Conversion costs are high—£1,600-2,000. It would take a typical motorist three or four years to recoup those costs, although a high-mileage motorist would do it sooner.

Policy mistakes haven't helped. In other countries subsidies helped to kick-start demand, but Britain's system of conversion grants was badly run, and eventually fell foul of European state-aid rules.

Nevertheless, ministers are keen to promote gas for cars on environmental grounds. The government has introduced laws to establish standards for garages carrying out conversions. It has promised to keep LPG lightly taxed, which could help to convince big fleet operators to switch. Most LPG vehicles are exempt from London's city-centre congestion charge. All that has helped to boost demand, says Mike Chapman of the LPG Association.

Yet the RAC Foundation, a motoring research organisation, thinks that petrol-electric hybrid cars, such as Toyota's Prius, may be a better bet in the long run. Sales in Britain are modest, but growing fast:

Toyota sold 1,588 Priuses last year and expects to sell more than twice as many this year. Other manufacturers are joining in. At the moment, says Edmund King, the RAC Foundation's executive director, hybrids are expensive, but they offer advantages that LPG cars lack: drivers can use the existing network of filling stations, and hybrids are much more fuel-efficient. “I think we'll soon have a hybrid that's cheap, stylish and efficient,” he says. “Then the market will really take off.”

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Drinking laws

Sobering

Aug 11th 2005
From The Economist print edition

Dire predictions about the consequences of deregulated drinking

NEW Labour has more of a reputation for nannying than for liberalism. An existing ban on foxhunting, a looming one on smoking in public places and a mooted plan to restrict sales of unhealthy food are three recent examples. When ministers do occasionally flirt with liberalisation, they tend to regret it. Plans to deregulate gambling were hastily scaled back after howls of outrage. Plans to liberalise Britain's archaic drinking laws by allowing pubs to close later are equally troubled.

Ministers hope that late opening will curb alcohol-related violence by preventing thousands of drunks being ejected on to the streets at the same time. They look longingly at southern Europe where, they say, liberal licensing laws are part of the reason for the cultured and brawl-free nightlife. Plans to change the system date back to Labour's first term, when they were mostly uncontroversial. Yet now, with the new regime only three months away, almost everybody is opposed.

On August 10th a group of senior judges claimed that the laws would cause a big rise in violent crime, and dismissed the government's hopes for cultural change as “wishful thinking” and “close to lunacy”. They want big hikes in alcohol taxes (already some of the highest in Europe) to discourage consumption.

The Association of Chief Police Officers, which supported late opening at first, has also come out against the plans. It says that unless the government provides better infrastructure—more public toilets, extra buses and trains to take revellers home, and, bizarrely, late-opening kebab shops—British high streets will come to resemble nasty Mediterranean holiday resorts, awash with drunken youths fighting and having sex.

Some local authorities that had supported the “24-hour city” concept in the 1990s have cooled on the idea of drinking into the small hours. Westminster Council, the country's biggest licensing authority, says that changing the laws will not change behaviour. It wants a rethink of the entire policy.

The government continues to argue the case for liberalisation, saying that the actions of a small minority should not prevent Britons from enjoying a late-night tipple. It points out that new powers will be given to local councils to close down troublesome nightspots and that a planned levy on rowdy drinking dens could help offset the extra cost of policing them.

The British Beer and Pub Association, a trade group, insists that fears of lawlessness are overblown. Most of its members want to extend their opening times only by an hour or two. It points to Scotland, which has more liberal regulations than England. There, a recent review recommended against statutory closing times.

Yet the worriers have an example of their own. In 2000, Ireland tried a limited experiment with loosening its licensing laws, allowing pubs to open for an extra hour on Thursdays, Fridays and Saturdays. Cases of fighting and drunkenness rose.

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Europe and terrorism

The French lesson

Aug 11th 2005 | PARIS
From The Economist print edition

Eyevine

European countries considering tougher anti-terrorism measures are increasingly looking to France for an example

Get article background

SINCE the London bombings, all European governments have been re-evaluating their counter-terrorism strategies. Many have been studying France, which has both experience of Islamist terrorism and a reputation for toughness. Right on cue, the French government has promised a new anti-terrorism law by the end of this month, designed to strengthen the hardline approach that it has put in place over the past ten years.

Nicolas Sarkozy, the interior minister, sums up this approach as “zero tolerance”. It has three broad elements. The first is increased surveillance. Thanks to the Renseignements Généraux, the second domestic intelligence agency, a network of agents has for years monitored Muslim activity, especially since the 1995 Paris bomb attacks by Algerian terrorists. Of the country's 1,600 mosques and prayer places, the RG reckons that perhaps 50, mainly in Paris, Lyons and Marseilles, are under the influence of radicals, mostly Salafists. Although only a few of these actually advocate violence, Dominique de Villepin, the prime minister, has long argued that all radical preaching is susceptible to calls for terrorism, so close monitoring is essential.

It is also now recognised that terrorist recruitment may no longer take place in official places of worship, but rather in private apartments, Islamic bookshops, fast-food joints, even rural retreats. The intelligence agencies are particularly worried about three groups: converts to Islam, citizens who have fought in Iraq and brought back violent ideas, and those who are radicalised in prison. France's Muslims make up under 10% of the total population, but a majority of prisoners, says Farhad Khosrokhavar, author of a study on the subject.

For a country that has few hang-ups about surveillance, France uses relatively little machinery to monitor what people are doing. There are 6,000 CCTV cameras on the London Underground alone, but only 900 that record permanently on the Paris Metro and RER rail network. After seeing their value in London, Mr Sarkozy plans to install cameras throughout the capital's public-transport system. His new law will lengthen the time that such film is kept, currently only a month. And mobile-telephone firms will be required to keep records for at least a year.

The second element in France's approach might be termed “offensive harassment”. The French have long been exasperated by what they see as excessive tolerance of radical Islam in Britain. They prefer active intolerance. The authorities often raid places suspected of harbouring extremists. The pretext may be anodyne: a health and safety check, a tax audit. According to a leaked RG report, 88 such raids were made in the Paris region alone last year, on restaurants, butchers, long-distance telephone shops and the like, involving 1,173 people. Of these, 185 were taken into custody, and eight prosecuted.

The point is not necessarily to uncover acts of violence in preparation, but to deter any such activity in the first place. “One cannot quite imagine Anglo-Saxon countries imitating our tactic of harassment, sometimes without real elements of proof,” Alain Chouet, former head of France's external-intelligence agency, told *Le Figaro*. “Sometimes it's a bit borderline, but it upsets the networks, prevents them from taking action.” No changes to this policy are planned, but liberal opinion seems readier to accept it than it once was.

The third element is a tough criminal-justice system, long predating September 11th. Suspected terrorists can be held for 96 hours without charge. A 1996 law gives judges free rein to detain suspects merely for “association with wrongdoers involved in a terrorist enterprise”. The four French suspects released from Guantánamo Bay last year were immediately detained on their return to France. The justice minister, Pascal Clément, plans to toughen this law, lengthening the penalty for such association from ten to 15 years.

France also takes a hard line over expulsion of radical clerics. This policy, begun when Mr de Villepin was interior minister, is now being stepped up. Mr Sarkozy expelled two Algerians in July. One, Abdelhamid Aissaoui, a young preacher accused of encouraging jihadists, had already been sent to prison for his role in a 1995 attempted bombing near Lyons. The other, Reda Ameuroud, was deported after calling for *jihad* in Paris. Mr Sarkozy told *Le Parisien* that “we must act against these radical preachers who are capable of influencing the youngest and weakest-minded.” He expects another dozen preachers to be expelled by the end of August, and he is considering withdrawing the citizenship of any French nationals involved—though it is far from clear where such non-citizens might then be sent.

Other countries are acting along the same lines as France. Britain is considering new anti-terrorism laws (see article). Germany, which already has a muscular set of legal tools left over from the years of left-wing terrorism in the 1970s, has passed even tougher measures recently. After the Madrid bombings, it enacted new laws to make it easier to deport those preaching *jihad*. Recently the interior minister, Otto Schily, has suggested giving German federal police additional powers to act pre-emptively and to let judges order the detention of suspected terrorists even without a conviction.

Yet the reaction to this last proposal shows that there are limits to how far Germany will go. Mr Schily, who as a lawyer once defended alleged terrorists himself, took much flak for his idea, with its shades of Guantánamo; some suggested he had forgotten the lessons of the Third Reich. The courts, too, are raising red flags. The Constitutional Court recently struck down legislation in Lower Saxony that allowed preventive eavesdropping on telecommunications, and the judges declared unconstitutional a law implementing the European arrest warrant, allowing a suspect wanted by Spain to go free.

Europe in general, and France in particular, prides itself on being the birthplace of human rights. Yet the repressive legal armoury in France prompted barely a murmur of liberal protest even before the London bombings. There is little to match public demands in Britain that foreigners who are thrown out must not face ill-treatment at home—French magistrates tend to accept at face value assurances that this will not happen. Indeed, the French request for the extradition from Britain of Rashid Ramda, wanted in connection with a 1995 Paris bomb attack, was resisted by his lawyers on the ground that he might be ill-treated in France. The French seemed happy to forgo some civil liberties in the name of security, even before the latest terrorism threat. In today's climate, other Europeans are starting to think similarly.

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Germany's election

Wagging the west

Aug 11th 2005 | BERLIN
From The Economist print edition

How the east will determine the outcome of Gerhard Schröder's gamble

Get article background

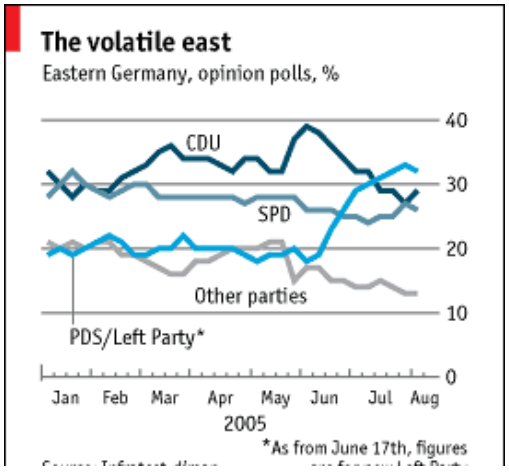
IF GERMANY were still divided into communist east and democratic west, the outcome of its election next month would be clear. The Christian Democrats (CDU) and the Free Democrats (FDP) would win a comfortable majority, with the outgoing coalition of Social Democrats (SPD) and Greens falling below 40%. And the new Left Party would struggle to cross the 5% threshold for seats in parliament.

Since unification, however, politics in Germany has become more volatile. In recent weeks, the overall CDU/FDP lead has been slipping, especially in the five states that made up the former East Germany (minus Berlin). It is not, as some assert, that elections are won in the east; but they can certainly be lost there. It is this, not the fact that Angela Merkel, the CDU's candidate for chancellor, comes from the region which explains why the east looms so large in the current campaign.

The eastern states have around 11m voters, fewer than in North Rhine-Westphalia alone. More important than voter numbers is the strength of the local ex-communist party, which has now joined with a western partner to form the Left Party. Yet what makes the east's voters really count is that they are so fickle. In the west many voters stay loyal to one party (though less than in the past); in the east they change their minds according to the issues or the candidates. This year, each of the three main parties has topped the opinion polls in the east at least once.

Despite the east's importance in elections, most western politicians tend to ignore it the rest of the time. The east's economic and social woes have played little recent role in German politics. Chancellor Gerhard Schröder declared in 1998 that the east was a “matter for the boss”, but he soon lost interest. Yet he is the politician who has benefited most from the east. In 1998, he won in large part because voters in the east were disillusioned with his predecessor, Helmut Kohl, who had promised them “flourishing landscapes” after unification. Four years on, Mr Schröder won again, thanks to catastrophic floods in the east and the looming war in Iraq (the first allowed Mr Schröder to show solidarity by offering prompt aid, the second let him demonstrate his pacifism, a value that resonates in the east).

Things will be different this time, even though the SPD has regained some ground in the east (as it has in the west). Voters in the east remain disappointed by the government's economic and employment failures—and this is unlikely to change by polling day. The big question is whether they will opt instead for the CDU, or for the Left Party. At present, the Left Party has the upper hand: the polls put it ahead of both the CDU and the SPD in the east (see chart).



Source: Infratest-dimap are for new Left Party

Contrary to what one might have expected, given her origins in the east, Ms Merkel is not an asset for the CDU there. In fact, more voters in the east would prefer to keep Mr Schröder than to give her a chance. This is because she is not seen as an *Ossi*, but as just another western politician. There is not much she can do about this: if she plays the card of her roots or runs a special campaign in the east, as some have suggested she should, she risks losing votes in the west.

It does not help that Jörg Schönbohm, a western CDU politician who is now a minister in Brandenburg, recently blamed the “forced proletarianisation” of the east's rural population under the communists for the case of a mother who had killed nine of her babies soon after their births. He was criticised for seeming to suggest that killing babies was typically eastern behaviour. Edmund Stoiber, the leader of the CDU's Bavarian sister party, also caused a stir by attacking the east's political influence, saying “the frustrated cannot determine Germany's future.”

Ms Merkel's best bet may lie in presenting herself as proof that change—and thus further reforms—are necessary and can lead to success. As the weekly *Die Zeit* recently noted, it would be a huge historical irony if Ms Merkel became Germany's first eastern chancellor since unification, but still lost on her home turf against barely reconstructed former communists.

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Greece and Turkey

Mission to Ankara

Aug 11th 2005 | ATHENS
From The Economist print edition

The troubles affecting Greek support for Turkey's EU aspirations

COSTAS KARAMANLIS would like to be the first Greek prime minister in half a century to make an official visit to Turkey. Besides demonstrating the positive shift in Aegean relations, a trip would put a stamp on Mr Karamanlis's own contribution. His centre-right government has consistently backed Turkey's desire to join the European Union. And he gets on well with Recep Tayyip Erdogan, the Turkish prime minister, a fellow soccer enthusiast.

The official visit was first planned for June, but Mr Karamanlis was persuaded to wait until August, when Turkey should have cleared the last remaining hurdle to the start of EU membership talks on October 3rd: signing the protocol extending its customs union with the EU to the ten new members that joined last year, including Cyprus. Yet last week Mr Karamanlis called off his visit again. Turkey had signed the protocol, but also issued a statement that this did not imply recognition of the Greek-Cypriot government.

Such non-recognition, declared Yannis Valinakis, Greece's deputy foreign minister, “will cast a shadow over Turkey's accession talks.” Greek enthusiasm for Turkish membership may wane if Turkey keeps refusing to recognise the Greek-Cypriot government. The stakes were raised last week when France's prime minister, Dominique de Villepin, said it was “inconceivable” that membership talks could begin with a country that did not recognise all 25 members of the EU. This week the European enlargement commissioner, Olli Rehn, responded that new conditions could not be set for the start of entry talks.

In this confusing situation, Mr Karamanlis reluctantly called off his visit. He is worried about losing popular approval if he seems not to care about Cyprus, or to care less about it than France does. The island remains divided after the Greek-Cypriots voted overwhelmingly against the UN reunification plan in a referendum in April 2004 (the Turkish-Cypriots voted in favour). Showing solidarity with Greek-Cypriots, even though they shot down the UN plan, counts in Greek public opinion.

Cyprus is not the only issue. Nationalist Greeks are quick to respond to pin-pricks, which often involve the Turkish armed forces; for example, there have been renewed Greek complaints of airspace violations. Turkey is resisting pressure to reopen a seminary for Greek Orthodox priests on the island of Heybeli, near Istanbul, an issue that Greeks see as a benchmark for assessing the Turkish government's commitment to EU standards of human rights and religious freedom.

Among Greeks, there is still a widespread desire to see Turkey following a European road to respectability and regional peace. Since Turkey became an EU candidate, the Greek and Greek-Cypriot governments have both cut defence spending sharply. A Europeanised Turkey would relieve deep-seated feelings of insecurity in Athens and Nicosia about Turkey's large size and powerful army.

In practical ways, too, Greek-Turkish rapprochement is steaming ahead. Mr Karamanlis and Mr Erdogan met in July, on the border in Thrace, where they initiated the construction of a pipeline to carry gas from Turkey via Greece to Italy—their first cross-border infrastructure project. Many well-off Greeks now take holidays on Turkey's Aegean coast, where five-star hotels are cheaper and offer better service than on many Greek islands. There is talk of a Turkish conglomerate buying a stake in a Greek-owned oil refinery. If Turkey starts its EU talks in October, Mr Karamanlis may yet get to Ankara—and into the history books—before the year is out.

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The Russian navy

Potemkin fleet

Aug 11th 2005 | MOSCOW
From The Economist print edition

Reuters

The good news, and the less good news, from Russia's submarine drama

THEY survived. That was the big difference between Russia's latest maritime drama, in which, thanks to help from a British naval rescue team, seven men were saved after their mini-sub got into trouble off Kamchatka, and the *Kursk* tragedy five years ago, when 118 sailors died at the bottom of the Barents Sea. But in other ways the comparison was not encouraging.

The men survived because the Russians accepted foreign help at a moment when it could still make a difference. Five years ago they waited until there was no hope, and also tried to blame a non-existent foreign craft for hitting the *Kursk*. The psychological cost to Russia's top brass of last week's humility was considerable. But it is too soon to conclude that this reflects a new priority for human life over pride and secrecy.

As with the *Kursk*, the authorities issued contradictory information: this time, about how much air the men had left, and about exactly what had entangled their mini-sub (a combination of fishing nets and a surveillance system, it seems). At least one of the sailors' relatives reportedly heard about the drama only through the media. A naval psychologist is said to have encouraged her with the words, “This is Russia: pray!”

The biggest unchanged thing is the Russian navy itself. It plans to buy some of the remote-controlled gadgets used by the British rescuers. But, as Pavel Baev, a military analyst, says, the navy is in such poor shape that accidents of this sort are “doomed to happen again and again”. Between the *Kursk* and this week, another submarine sank in 2003, with nine lives lost. Last month, the flagship of a naval review in St Petersburg was damaged during a rehearsal.

The problem is that, even as the navy has shrunk from its Soviet size, the admirals still like to pretend that they can fight on the high seas, rather than using their limited means to prepare for more plausible tasks such as preventing poaching, or to care for and train their sailors. Mark Galeotti, of Britain's Keele University, says the result is a Potemkin navy, which can “just about pass muster so long as nobody shoots at it.”

Another similarity with the *Kursk* was the invisibility throughout the crisis of Vladimir Putin, Russia's president. For all his posturing and would-be authoritarianism, avoidance of responsibility is still an imperative for Mr Putin. Weakness and neurosis beneath a semblance of power: the president and his navy have much in common.

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Sweden's government

Undesirable Persson

Aug 11th 2005 | STOCKHOLM
From The Economist print edition

The Social Democrats face an uphill struggle to win next year's election

AFP

THE short Swedish summer is over by mid-August. As Goran Persson, the Social Democratic prime minister, returns to the political fray, he faces a long autumn trying to revive his party's fortunes. Just over a year before the next election, combined support for his minority government and its allies, the Left and Green parties, is at its lowest for a decade. After 11 years—indeed, after being in power for all but nine of the past 73 years—the Social Democrats are finding it tricky to persuade voters that they haven't run out of steam.

To an outsider, this may seem odd. Compared with most other European countries, Sweden's economy is in good shape. High-tech industry is booming. The public finances are in surplus. Last year GDP grew by 3.5%. Growth this year is expected to be nearer 2%, but that is still faster than most euro-area economies. Inflation remains low and, with Sweden outside the euro, the central bank was able cut interest rates to 1.5% in June.

The cloud is that unemployment remains stubbornly above the government's 4% target. An unadjusted figure of 7.1% in June is not that high by European standards, but many economists believe that the true number who cannot find work is a lot bigger. It is masked by liberal use of make-work schemes, further education, early retirement and sick leave—on as much as 80-90% of previous salary. Employers fearful of such costs are understandably reluctant to hire. The spectre of jobless growth haunts a government that has promised to cut unemployment.

The Social Democrats have also been hit by a string of petty scandals, ranging from the fiddling of membership records in its youth wing, so as to secure bigger grants, to the abuse of housing perks. None of this is big enough to claim a ministerial resignation, still less a prosecution, but enough to gnaw away at the trustworthiness of a party that is used to running the country. Public bickering within the local Stockholm party has not helped.

What of Mr Persson himself, now in his tenth year as prime minister? Remarried and with a recently acquired country estate to renovate, his enthusiasm for the job has been questioned. He is respected rather than liked. In April, he hinted that he might be willing to step down. But he has no obvious replacement. The murder of his foreign minister, Anna Lindh, in 2003 robbed the party of a natural successor. Margot Wallstrom, Sweden's European commissioner, with whom Mr Persson has an icy relationship, has ruled out a return to domestic politics.

In contrast, the opposition has been reinvigorated by Fredrik Reinfeldt, the leader of the conservative Moderates, the biggest of the four main opposition parties. Mr Reinfeldt has dragged the Moderates to the centre, dumped the ideological tone of his predecessors by, for instance, reducing the party's zeal for tax cuts. His emphasis is on reforming, not scrapping, the Swedes' much-cherished welfare model. It may be too early to count the Social Democrats out: Mr Persson remains a formidable campaigner. But he faces a tough task to persuade Swedish voters to give him and his party another four years in the sun.

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The Czech police

Bonking ravers

Aug 11th 2005
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Policing and politics make an inflammable mixture

AFP

Whose side are you on?

THE Czechs are admirably orderly, and they also revere music and detest violence: police brutality against student demonstrators in Prague in 1989 sparked the revolution that toppled communism. So when 1,000 riot police recently broke up CzechTek, a rave attended by 5,000 fans in the Bohemian countryside, causing dozens of injuries on both sides, reactions were strong—and contradictory.

The liberal-minded intelligentsia, and most young people, were outraged. Protests are continuing almost two weeks later. In the Senate, which debated the matter for five hours, politicians compared the ravers to the student victims of communist-era police, and noted that the roots of the 1970s dissident movement lay in underground popular music.

The critics are not just young or nostalgic. They include the right-of-centre opposition party and its foremost figure, President Vaclav Klaus. A square lot that have never shown the slightest sympathy for druggy, hairy youth culture, they are unlikely allies. But they want to embarrass the centre-left government, and especially the prime minister, Jiri Paroubek. Mr Klaus said the authorities had made a "gross mistake" and demanded a formal explanation.

The police have plenty of supporters, however. The Czechs are fed up with the antics of foreign holidaymakers, especially young ones, for whom the country is central Europe's best and cheapest fleshpot. An illegal rave last year was highly disruptive. This one, on a rented piece of land, led to the trampling of nearby private property, police said.

Mr Paroubek played the law-and-order card hard. It was offensive, he wrote in a newspaper, to compare the ravers to the youthful heroes of 1989, "who took to the streets with an exalted human message". The techno-rave fans were "obsessed people with anarchist proclivities and international links" who "provoke massive violent demonstrations, fuelled by alcohol and drugs, against peaceful society."

Yet an opinion poll suggests that, though Czechs are evenly divided as to whether the police should have broken up the rave, some 70% believe the tactics used were too rough. Mr Paroubek has since softened his tone, promising to make changes in the law governing local authorities' powers to manage such gatherings. The protests may fizzle out, but worries about the scandal-plagued police will remain. Many Czechs feel that the force's enthusiasm for truncheons is not matched by an ability to solve crimes, fight corruption or protect the public.

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The economy

By the numbers

Aug 11th 2005 | WASHINGTON, DC
From The Economist print edition

The economy's prospects look rather good. George Bush's don't yet

Get article background

ALL presidents, whatever their confession or denomination, are closet numerologists. Numbers are how they read the mood and track the progress of the nation they govern. For George Bush, the numbers—rising casualty rates in Iraq, falling approval ratings at home—have not been good of late. Hence he is turning with some enthusiasm to a happier set of figures: those tracking the American economy's resilience and resurgence.

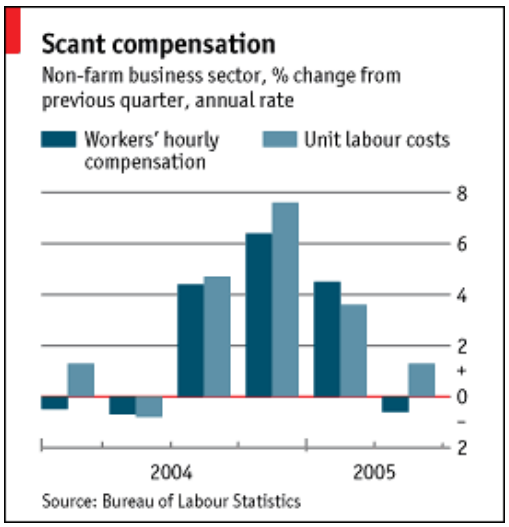
This week, he summoned his economic team to a meeting at his ranch in Crawford, Texas. Under a painting of a rodeo, they discussed an economy that is kicking strongly, but not bucking out of control. Output grew at an annual rate of 3.4% in the second quarter, a little slower than in the first. This was largely because firms chose to run down their inventories (subtracting 2.3 percentage points from growth) rather than making new stuff. With their shelves now depleted, companies are expected to restock in the coming months and output is expected to rebound. Some analysts now forecast growth of 5% this quarter.

Momentum is gathering. Cars left the showrooms at a near-record rate in July (20.8m a year), and existing home sales reached all-time highs the month before (7.3m a year). Factories reported faster activity and fuller order books, especially for capital goods (up by 3.9% in June) that presage stronger investment. Even the federal government is doing well. So far this fiscal year, it has collected about $210 billion more in taxes than it had by this time last year.

Best of all, hiring is steady and sure. Employers added 207,000 workers to their payrolls in July, and 42,000 more than previously thought in May and June. They have hired about 200,000 workers a month on average since the end of January—not spectacular by the standards of the 1990s, but a marked improvement on Mr Bush's first term.

The Federal Reserve has digested the same numbers as Mr Bush and reached a similar conclusion. There is much to welcome and little to fear in the economy's current progress. This week, as widely expected, it raised interest rates by a quarter-point. It has now made ten such “measured” steps since June 2004. Judging by the statement accompanying its decision, it looks set to make more such steps.

Unlike central bankers and presidents, the public at large sets little store by numbers. Only a fifth of those polled recently by CBS News thought the country's economic fortunes were improving, whatever the statisticians might tell them. More than half disapproved of Mr Bush's handling of the economy.



What explains their scepticism? In Mr Bush's first term, he was dogged by the question: Where are the jobs? Now the question is: Where are the pay rises? Workers' total compensation grew strongly for the three quarters that began in July of last year (see chart)—strongly enough to alarm some of the inflation hawks at the Fed. But these gains were probably not very widespread, confined to those lucky employees who collected juicy bonuses or cashed in their stock options. Last quarter, according to figures released on August 9th, compensation actually fell, in real terms. This will reassure the Fed for now. But Mr Bush may be less pleased: better paid workers are happier voters.

Indeed, the picture is worse for workers than these figures imply. Not all of an employee's compensation ends up in his pay packet. Much of it goes in the form of benefits, such as employer contributions to health insurance or pensions. According to the Bureau of Labour Statistics, the cost of such benefits accounted for almost 60% of the gains in compensation enjoyed by private-sector workers in the first quarter of the year, and nearly 35% of the gains in the second. By the bureau's reckoning, wages and salaries proper grew by only 2.4% in the year to June, slower than the rate of inflation.

Despite these meagre pay gains, households are eager to spend whatever they get. In June, they earned just over $9 trillion (at an annual rate) in disposable income. They duly disposed of all but $1.9 billion (0.02%) of it. Only in the month after September 11th, when shopping was deemed a patriotic duty, has the household saving-rate been lower. Households save so little of what they earn because they gain so much from what they already own. In the 12 months to March the value of their houses rose by $2.3 trillion, according to the Fed. Home prices rose by almost 15% in the year to June, the fastest in decades.

Can these gains continue? Judging by the minutes of its recent meetings, the Fed is agnostic about the existence of a bubble in the housing market. One simply cannot know for sure, it says. Even if a bubble does exist, the Fed believes it should do little about it. America's central bank is making the opposite of Pascal's wager: one cannot know whether an almighty bubble exists, so one should act as if it doesn't.

As for Mr Bush, he began his second term with the bold idea of reviving thrift in America. By reforming taxes and entitlements, he would encourage industry and frugality. Those ambitions are currently entombed in Congress and his own weakness. If it had stuck to its original schedule, his commission on fundamental tax reform would have reported by now. Instead, Mr Bush postponed its report to give himself time to sell his Social Security reform. Unfortunately, if he continues to wait for that sale to be made, the commission may never report at all.

Mr Bush's economic team now has more modest yardsticks for success. It is proud of the 217 votes it wrung out of the House of Representatives last month to secure passage of the Central American Free Trade Agreement. It is also pleased with China's small revaluation of its currency, which has bought some respite from the protectionists in Congress. Even the $286-billion transport bill—which Mr Bush once threatened to veto, but this week seemed happy to sign—is being hailed as a legislative success. Roads and bridges, not the “third rail of politics” (as Social Security is known), are about the summit of

his current ambitions.

Mr Bush still has more than three years to achieve his grander goals of reforming taxes and overhauling entitlements. But before he can hope to transform the American economy, he must hope the economy's good numbers transform his own flagging ones.

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Inner-city poverty

The problem with ghetto grocers

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It's costly being poor

THIS week saw the start of yet another campaign to boycott Wal-Mart. In Philadelphia, the United Food and Commercial Workers (UFCW) joined two teachers' unions to urge parents not to buy their school supplies at the big store, which doesn't recognise unions. “Low wages mean more poverty,” announced the UFCW's local chief.

Yet the poor might benefit from low prices. “The Price is Wrong”, a recent report from the Brookings Institution, a think-tank based in Washington, DC, found that Philadelphia's poor pay more for almost everything than the city's rich folk do: they pay more for loans because their credit history is patchier, more for insurance because their neighbourhoods are rougher, and more to cash cheques because they don't have bank accounts and go to extortionate cheque-cashing stores that can bite $450 a year out of a household income of $15,000.

And they pay more for their groceries because they shop at places like the Thrift Discount store on Girard Avenue. Wal-Mart, it ain't. There's not much choice, the soup cans are grimy with dust and the nappies are 57% dearer than at a big store in the suburbs.

Why doesn't somebody undercut Thrift Discount and its sort? One reason is the powerful lobby against big stores, such as Wal-Mart, opening in cities. Another is that small entrepreneurs don't like working in rough neighbourhoods. “It's not so bad round here during the day, but you hear gunshots every night,” says Patrick Park, a member of the Korean-American family that owns Thrift Discount. Armed robberies are fairly common in the area, he says, and shoplifting is “a big problem”.

Brookings says the risks of running shops in poor areas are exaggerated, citing a Department of Agriculture report that found no statistically significant differences in operating expenses between grocery stores in poor and rich areas. Poor densely populated areas also contain more potential shoppers. Heidi Hwang, Mr Park's sister, who is minding the till, says she is astonished how many $50 hair extensions she sells.

One intangible and awkward cost glossed over in the Brookings report is the daily experience of racial tension. “They don't like us watching them,” says Ms Hwang, “but then you turn your back and they steal something.” Black shoppers have a different perspective. Ice Cube, a rap artist, once released a song called “Black Korea” that included the lyrics: “[D]on't follow me up and down your market/Or your little chop-suey ass 'll be a target” and “[P]ay respect to the black fist/Or we'll burn your store, right down to a crisp.”

Such threats are very rarely carried out, of course, but they are another reason why shopkeepers shun the inner cities. Mr Park's family moved to the suburbs as soon as they could afford it. And Mr Park says he won't take over the family business unless he has to. He's planning to be a lawyer.

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The United Nations

A nasty smell

Aug 11th 2005
From The Economist print edition

The oil-for-food mess is complicating hopes for reform

AP

Sevan on the spot

Get article background

"IMAGINE an American administration in which the attorney-general secretly derives nearly half his income from the Gambino crime family. Imagine, too, that this hypothetical attorney-general is a longstanding confidant of the president." This is how the editorial page of the *Wall Street Journal* invites readers to think of the United Nations under Kofi Annan.

In fact, this week's report into wrongdoing at the UN'S oil-for-food programme in Iraq reads more like a John Grisham thriller than "The Godfather"—but it is hardly edifying stuff. There are shell companies, Swiss banks, stacks of hundred-dollar bills and Panamanian companies with "directors" who do no work.

According to the investigation, which was led by Paul Volcker, a former chairman of America's Federal Reserve, Benon Sevan, the head of the oil-for-food programme, "corruptly benefited" from $150,000 in kickbacks from a friend's oil company. The report also alleges that a Russian in the UN's procurement division, Alexander Yakovlev, solicited bribes to help an inspection contractor win a bid. Mr Yakovlev has pleaded guilty, but Mr Sevan has denied any wrongdoing.

The oil-for-food scandal has been rumbling on pretty much since Saddam Hussein was deposed. This is the first time that Mr Volcker's commission, which was set up by Mr Annan, has claimed unambiguously that UN officials have been on the take. American conservatives have seized on it as proof that the UN is mismanaged.

Coincidentally, those same conservatives are the ones who make most fuss about reforming the UN. It so happens that, next month, the biggest-ever summit of world leaders in the UN's history will take place to discuss precisely that. The 60th annual session of the General Assembly will consider a basket of proposals to modernise the UN. The prospects are dim.

The bitterest squabble concerns enlarging the Security Council from its present five permanent members, the United States, Britain, France, Russia and China, and expanding the number of non-permanent ones, in order to better represent the world. Four of the most credible claimants to permanent-member status—Germany, Japan, India and Brazil (G4)—have just been disappointed by their failure to find allies in the African Union, which voted the idea down in a full session last week.

Even if the G4 and Africa fell back into step, there would be no guarantee of success. Local rivals of the G4 (such as Argentina, South Korea and Italy) are frosty about their elevation. And one of the permanent five could veto enlargement. China is not keen on Japan, and America is still upset with Germany for opposing the Iraq war. Hence the rumour that George Bush's controversial new ambassador to the UN, John Bolton, and his Chinese peer are working together to scotch any enlargement. American officials deny that, but they are hardly pushing expansion either: in a one-page press release of six reforms it would like to see, the enlargement of the Security Council rates only a footnote.

There is talk of a compromise, with a new tier of members that might serve long temporary terms of up to 12 years. But America's opposition is not just bloodymindedness. A forthcoming study by Simon Chesterman of New York University points out that a more representative Security Council might be fairer, but not necessarily more effective; efficiency could be helped more by greater transparency, as well as more copious resources (including more peacekeeping troops).

Effectiveness, not representativeness, is America's main concern at the UN. Among its stated six priorities, the first, revealingly, is “budget, management and administrative reform”. Bills in the Republican-controlled Congress would make payment of American dues conditional on such reforms. The threat recalls the fight over unpaid American dues in the 1990s.

Other American priorities have broad support. These include a “peace-building commission” for war-torn countries, a new human-rights council that does not let countries like Libya and Sudan (as now) become members, a fund for promoting democracy and a definition of terrorism that would more tightly bind states to fight it. America also supports promoting development through corruption-fighting and sound economic policies.

Other UN members want these things too, but the G4 and the Africans want the Security Council to be the main project. The issue of development is also divisive. America wants to focus on corruption; others want to focus on the UN's goal of rich countries giving 0.7% of GDP a year in aid. And any mention about either the Kyoto protocol or the International Criminal Court irks the Americans. The oil-for-food scandal could provide a splendid pretext for everybody to do nothing.

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A mob family's last stand

Gotti go now?

Aug 11th 2005 | NEW YORK
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Do you know the difference between a restricted beating and a severe one?

WHEN prosecutors dropped a charge of conspiracy to murder against John “Junior” Gotti last month, leaving kidnapping, loan-sharking, extortion and stock fraud still on the sheet, a defence lawyer sniffed memorably: “We really only have a white-collar crime case.”

And perhaps it is, by the standards of the defendant's father, John senior. The head of the Gambino crime family was convicted of murder and racketeering in 1992 and died of cancer in prison ten years later. John junior, who was brought up in the family business, was completing five years' jail for racketeering when this latest batch of charges was brought last year. He went on trial this week, pleading not guilty and saying he had put crime behind him. “People can change,” insists his lawyer.

New Yorkers have not changed in the relish with which they follow such trials, timeless in their details. One snitch for the prosecution, Frank “Frankie Fapp” Fappiano, spent Tuesday explaining to jurors the difference between a “restricted beating”, with the hands, and a “severe beating”, requiring “a blackjack, a pipe, a baseball bat or a two-by-four”. The victim of the alleged kidnap, Curtis Sliwa, was the founder of the “Guardian Angels”, volunteers who patrolled the New York subway in the sink-like 1980s. He says he was grabbed and shot because he attacked John senior in a radio broadcast.

This may well be the Gottis' last courtroom drama. Last month Peter, John senior's older brother, was sentenced to 25 years in jail for ordering a failed hit on a Mafia turncoat called Salvatore “Sammy the Bull” Gravano, who helped convict his brother. Mr Gravano got five years' jail for 19 admitted murders, then abandoned his witness protection plan in Arizona to promote a book about his life. Prosecutors said Peter Gotti wanted him killed with a landmine or a hunting rifle, but Mr Gravano was arrested on drug charges before the plot could be carried out.

As ever, reality television offers an afterlife. Victoria, John junior's sister, stars in a successful show called “Growing Up Gotti”, which begins a third season this month. She and her mother, also called Victoria (they are not an imaginative family, names-wise), were both in court this week and on message. “Young John is a very tough guy, and he's proven it by his time in prison,” said Victoria senior, “but he doesn't want this life.”

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Skiing in Montana

The battle of Bitterroot

Aug 11th 2005 | MISSOULA
From The Economist print edition

A row over a bid to build the largest ski resort in North America

"THIS will be a wonderful pedestrian, easily walkable village," says Tom Maclay. He is gesturing at a field of dried grass, off to the side of a bumpy dirt road. Mr Maclay, a soft-spoken fifth-generation Montanan, has grand plans for his 2,900 acres of land in the Bitterroot Valley in the western part of the state. Already he has begun cutting trees for 30 ski runs (there will be a golf course for the off-season). He hopes to get a permit to expand into adjoining federal land managed by the Forest Service, thereby creating the largest ski resort in North America.

Don't buy those lift passes just yet. Alas for Mr Maclay, the site of Bitterroot Resort is just a few miles from Missoula, a leftish college town whose many green inhabitants are outraged by the idea that the valley will end up like Aspen or Jackson Hole. "It's almost not cool to have money here," claims Adam Switalski of Montanans for Quiet Winter Recreation, an advocacy group. A big resort would make house prices and taxes rocket. Gated communities would descend.

Mr Maclay replies that development is inevitable. Montana already has two big resorts, called Big Sky and Big Mountain (see map), as well as several smaller ones. The site near Lolo Peak, as the 9,096-foot mountain is called, has been studied twice by the Forest Service in the past 40 years but rejected for water reasons; Mr Maclay says that his proposal fixes this. He argues that Bitterroot Valley has the right infrastructure—a good airport and a four-lane highway—as well as a keen ski population.

To help with the planning, Mr Maclay has brought in Jim Gill, a former Jackson Hole executive. By developing his own private land—limited skiing will be available, though not yet with chairlifts, this winter—Mr Maclay seems to be hoping that locals will get hooked on skiing and change their minds. Getting the Forest Service to open up public lands is crucial, since the expert slopes lie near the top of the peak, well above his property line. If his proposal were approved, skiers would be able to descend 5,342 feet—the longest such vertical drop in the country.

But the clear-cutting of the runs, easily visible from the nearby highway, has energised opponents. "The absolute arrogance of it is really pissing Missoulians off," says Daphne Herling of an opposition group, Friends of Lolo Peak. The arguments run the gamut. A resort would divide the summer (high-elevation) and winter (low-elevation) grazing lands of a 125-head elk herd, says Bob Clark of the Sierra Club. It

would cut into one of the largest roadless areas in America, and invade a spot where unusual hybrid larch trees grow.

Then there is Lewis and Clark, always a trump card in Montana. The expedition camped in the Lolo area in September 1805 and noted the surrounding snow-capped mountains in their journals. So development would harm the historic view and be “almost a slap in the face” for this year's bicentennial celebration—or so claims the Sierra Club's Mr Clark.

Then there is the problem of snow. One small resort nearby, Marshall Mountain, did not open this year because it did not have enough of the white stuff. Mr Maclay admits he will have to make a lot of snow, but insists there is water to support it. The fact that the resort is north-facing (unlike Marshall Mountain) helps, and extra water stored on the mountain could help restore the watershed of the Lolo creek and its depleted rainbow trout.

The Forest Service must make a ruling. First, the agency is due to come out with a new draft of its land-use plan; after public consultation, that could be finalised next year. An answer to Mr Maclay's permit application would presumably come after that. If he is refused, his opponents fear that he and his developer chums will persuade one of Montana's three representatives in Washington, DC, to sneak a rider into another law. The battle of Bitterroot may drag on a while yet.

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Peter Jennings

Style and substance

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An anchorman who enjoyed explaining the world to America

"JOURNALISM should be fun," said Peter Jennings of his profession. For the urbane ABC anchorman, who died this week, that meant an infectious eagerness to know what makes the world tick, from middle-America to the Middle East. He edited and presented the network's evening news for 22 years, but at heart he was always a reporter and, especially, a foreign correspondent; one of his last jobs was to cover the Iraqi elections from Baghdad.

For some Americans the Canadian-born Jennings was, in fact, too foreign a correspondent. He played cricket as a schoolboy, wore a Scottish kilt to parties in Beirut and his second wife, out of four, was Lebanese. He took American citizenship only two years ago, while still retaining his Canadian credentials.

Clearly, he did not have the "down-home" American character of the other two members of the news triumvirate—NBC's Tom Brokaw and the folksy Dan Rather of CBS. Yet for a decade from the mid-1980s, he surpassed them both in the ratings, helped by a combination of worldliness, wit and objectivity (he never riled conservative Americans as much as Mr Rather did). The retirement last year of Mr Brokaw, who had snatched first place away from Mr Jennings, offered the ABC man a chance to recapture it from the less experienced Brian Williams—but then cancer struck.

By his own admission, Mr Jennings had been promoted too young. He was first given the job of ABC's anchor, at 26, largely on the basis of looks (providing, some said, the model for the hero of "Broadcast News"). After he had floundered against CBS's Walter Cronkite and NBC's team of Chet Huntley and David Brinkley, ABC cleverly sent him on postings to Rome, Beirut and London to "add a few lines" to his face. The years abroad, allied to a voracious reading habit, also provided intellectual ballast for a self-confessed "bone-lazy" student who had dropped out of high school.

Mr Jennings's success at ABC was set against the decline not just of network news (the average age of ABC's audience is now 60) but also of the journalism he enjoyed. Impartiality has given way to the stridency of Fox News and the internet bloggers. Meanwhile, foreign coverage is dwindling: last year, NBC's evening news show devoted just five minutes to the genocide in Darfur, CBS a mere three and ABC, thanks in part to Mr Jennings, 18. By contrast, they together devoted 130 minutes to the plight of Martha Stewart.

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Lexington

The jock-in-chief

Aug 11th 2005
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An old English idea has been reborn in the Bush White House

Get article background

THE phrase “muscular Christianity” is more resonant of Victorian England than modern-day Washington, DC. The idea was invented by British public-school headmasters (most notably Thomas Arnold of Rugby) who believed that a combination of sport and religion could develop the all-important quality of “character”. And it soon inspired generations of Englishmen to bring God and team sports to “lesser breeds without the law”. But today anybody looking for muscular Christianity would be advised to try the capital of the new American empire.

George Bush's well-known enthusiasm for God goes hand-in-hand with an equally well-marked enthusiasm for muscularity. Mr Bush is in “superior” physical condition, according to his annual medical. He can bench-press 185lb five times in a row; and, before a recent knee injury, he could run three miles at an average pace of six minutes and 45 seconds.

This “superior” condition is the result of an exercise regime that would have delighted Dr Arnold. Mr Bush's daily schedule is a secret, for obvious reasons; but whenever a calamity throws light on his routine he is invariably exercising. Earlier this year the White House was evacuated when an aeroplane wandered into restricted air space. Mr Bush was off mountain biking. In 2001, a lunatic fired shots at the White House. The president was working-out. In the morning before tragedy struck on September 11th Mr Bush had been running with a journalist who also happened to be a former All-American long-distance runner.

Mr Bush is a sports-fan as well as an exercise fiend. His greatest ambition, apart from being president, was to be baseball commissioner; his biggest, perhaps only, business success was as the managing partner of the Texas Rangers; and his favourite pastime is watching sports (he was watching American football when he had that bruising encounter with a pretzel). He is also keen on spreading his faith in physical fitness. In 2002, he launched a national fitness campaign by dragging 400 of his wretched staffers on a three-mile run.

Mr Bush is surrounded by fellow jocks. Donald Rumsfeld is a former Navy wrestling champion who, at 73, makes a habit of walking five miles a day through the Pentagon corridors. He also likes to challenge underlings to squash. Condoleezza Rice is a former competition-level ice-skater who rises at dawn to run on her treadmill. Margaret Spellings, the education secretary, is a weight-lifter. Even Alberto Gonzales, the diminutive attorney-general, is keen on golf and racquetball.

Enthusiasm for sport can be a ticket to Mr Bush's inner circle. Ms Rice works out with the president and spends time at Camp David watching baseball and football on television (apparently her most cherished dream is to be appointed the commissioner of the National Football League). And a poor physique can test the president's patience. When Mr Bush sacked Larry Lindsey, his portly economic adviser during his first term, he apparently complained in private about his failure to exercise.

Mr Bush's obsession was on full display during the search for a new Supreme Court justice. He apparently asked one candidate, Harvie Wilkinson, two tough questions: What is the most difficult decision you have ever made? And how much do you exercise? The 60-year-old Mr Wilkinson said he ran three and a half miles a day. But the president urged him to do more cross-training. “He warned me of impending doom,” Mr Wilkinson told the *New York Times*. In introducing the successful candidate, John Roberts, to the country Mr Bush highlighted the fact that he had been captain of his high-school football team—as if this made up for the fact that he was a swot at Harvard Law School.

Onward Christian athletes

The contrast with Bill Clinton could hardly be greater. You could hardly imagine Mr Clinton introducing Stephen Breyer or Ruth Bader Ginsburg as his Supreme Court nominees by citing their hockey skills. As for the president himself, his jogging was mostly for show, and a hefty hamburger would often be consumed afterwards. Mr Clinton much preferred nerds to jocks, and even gave the Pentagon to slouching Les Aspin.

Mr Bush's own likings are par for the course in his party. Look at the Republicans on Capitol Hill. Dennis Hastert, the House speaker, made his name as a high-school wrestling coach. Bill Frist, the Senate majority leader, is a keen marathon runner who takes his staff on workouts around the Mall. Another senator with presidential ambitions, George Allen, was a college sports star (and the son of a famous Redskins coach). And Arnold Schwarzenegger is, well, Arnold Schwarzenegger.

Or look at Republican voters. If the Democrats have an impregnable lead among the country's PhDs, the Republicans have a lock on the NASCAR crowd. For Democrats the main qualification for a top job is “intelligence”—hence their constant complaint that Republican presidents are too dumb for the job. But for Republicans the most important qualification is “character”—by which they mean an ability to hit balls and bang heads.

Mr Bush's preferences are also rooted in his family history. The Bushes have always made a point of sending their offspring to East Coast boarding schools that were modelled on Thomas Arnold's Rugby, where the chapel and the playing fields were carefully designed to inculcate muscular Christianity. Mr Bush's grandfather and father were both athletic stars (the 41st president played in the College World Series in both 1947 and 1948). A day at Kennebunkport is a mini-Olympics of tennis, swimming, horseshoes and high-speed golf.

This is not to say that all Democrats are nerds (John Kerry is a superb athlete), nor that all Republicans are jocks (Karl Rove is many things; athlete is not one of them). But therein lies the rub: unlike Democrats, Republicans are happy to let the jocks take the glory while the nerds do their homework for them.

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Correction: the SEIU

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In our piece on unions ("Losing its grip", July 30th), we said that the Service Employees International Union had 500,000 members in Canada; the correct figure is 76,000. This error was corrected online.

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Mexico's presidential race

The underdogs bare their teeth

Aug 11th 2005 | MEXICO CITY
From The Economist print edition

The front-runners have challengers snapping at their heels

Get article background

ASK any leading candidate in next year's presidential vote what he would seek to achieve if elected and the list tends to be much the same. More foreign investment to boost Mexico's flagging energy output; cuts in over-generous public pensions; a more efficient, “adversarial” judicial system modelled on America's; and of course, better education.

This is a contest not of ideas, then, but of personalities and party machines. Whoever wins, he is unlikely to enjoy a congressional majority. So one of the most important qualities in a candidate, besides the strength of the party apparatus backing him, is his perceived ability to persuade other parties' legislators to support what they would have supported anyway, had their own party's candidate won.

Since taking office in 2000, Vicente Fox, the serving president, from the conservative National Action Party (PAN), has failed spectacularly on this count. His heir-apparent, Santiago Creel, the interior secretary, looks no more promising. He is an uninspiring speaker and is considered politically inept. However, it is no longer clear that he will be the PAN's candidate. Felipe Calderón, a dynamic, young (43) former energy minister, has gained ground steadily and is now snapping at his heels.

A poll of PAN supporters commissioned by Mr Calderón shows he is now more or less tied with Mr Creel, having been 20 points behind ten months ago. Mr Creel's polls show his rival still trailing—but independent pundits think Mr Calderón's figures more reliable.

That Mr Calderón is a long-time PAN militant could hinder him, if the other parties' candidates successfully paint him as a time-serving apparatchik. Or it could help: Mr Calderón could be on to a winning formula if he convinces voters that his political savvy is the ideal complement to the technocratic competence with which he is already credited.

Anyone but Madrazo

Mr Calderón may have to fight other potential challengers, besides Mr Creel, for the PAN's nomination. Among them is Alberto Cárdenas, a former minister and state governor, whose star is also rising. But

success for Mr Calderón should boost the governing party's chances against tough challenges from its two main rivals. The statist Institutional Revolutionary Party (PRI) has the strongest party machine, having governed Mexico for 71 years until Mr Fox's election. And the expected candidate of the leftist Party of the Democratic Revolution (PRD), Andrés Manuel López Obrador—until recently Mexico City's mayor—is overall leader in the presidential polls.

Until recently it seemed almost certain that the PRI's boss, Roberto Madrazo, would be its candidate. However, earlier this month a group of party big-shots joined together under the slogan “Everyone United Against Madrazo” and endorsed a common candidate. He is Arturo Montiel, who is about to complete his term as governor of the state of Mexico (the country's largest).

The PRI's internal contest is as vicious as the PAN's is gentlemanly. Asked what was the main respect in which he differed from Mr Madrazo, Mr Montiel said: “I like to tell the truth.” It may indeed count against Mr Madrazo that the public widely perceives him as falling short of even Mexico's undemanding standards of probity in public life.

However, Mr Montiel must in turn shake off his reputation as an unreformed PRI old-liner, more interested in party gain than policies. He cheerfully admits that, in an election in July to choose his successor as state governor, his top priority was to ensure that the PRI stayed in power (he succeeded). Only then came his other main goals, fighting crime and poverty.

Mr Madrazo, as party chief, may also be able to fix its primaries to nobble his internal rival. That the PRI has not even set a date for them has strengthened suspicions that Mr Madrazo may be seeking ways to avoid an open challenge.

The rising underdogs of both the PAN and PRI stand the best chance of beating Mr López Obrador, especially if at least one of two other well-known figures join the presidential race. Cuauhtémoc Cárdenas, the PRD's failed candidate in three past presidential elections, may run for a smaller party. Jorge Castañeda, a former foreign minister, wants to run as an independent, though a Supreme Court ruling this week made this far more difficult. Neither stands much chance of winning but each could steal many votes from Mr López Obrador, whose position as the race's leader looks ever more fragile.

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Paraguay and the Moonies

Promised land

Aug 11th 2005 | ASUNCIÓN
From The Economist print edition

A town owned by a cult seeks liberation

ONE day in 2000 the people of Puerto Casado, a small town in Paraguay's inhospitable Chaco region, were shocked to learn that the ground had been sold under their feet—and that their new lord and master was the Rev Sun Myung Moon, the self-proclaimed messiah who leads the Unification cult, better known as the Moonies. Mr Moon's acolytes soothed locals' fears by promising all sorts of grand projects to make the town rich, from a meat-packing plant to an eco-tourism resort.

Five years on, with little sign of these promises being kept, hundreds of the town's people recently travelled 400 miles (640km) to the capital, Asunción, to lobby Congress to free them from the cult.

Earlier this month, the Senate approved a bill to seize some buildings and a slice of the Moonies' land, to share among the locals. Backing the bill, President Nicanor Duarte Frutos accused the Moonies of paying their local workers “starvation” wages (they say they pay the legal minimum). His Colorado party should muster enough votes to pass the bill in the lower house.

The Moonies claim the row has been whipped up by local politicians to extort money from them. This week they began selling their cattle and laying off workers, forcing Mr Duarte to announce an emergency aid package for the town.

Mr Duarte says the townsfolk are living in “semi-feudal” conditions. But things remain much as they were long before Mr Moon came along. The town was part of a vast estate that Carlos Casado, a swashbuckling Spaniard, bought from a desperate Paraguayan government in the late 19th century, after it had lost much of its territory and people in a calamitous war with Brazil, Argentina and Uruguay.

The town once made a good living from quebracho, a hardwood used to make tannin for the leather industry. By the 1990s, with the quebracho trees almost gone, the Casado company was looking to sell.

At this time, Mr Moon began buying land either side of the Paraguay river, on which the town lies. After discovering the region on a fishing trip, he decided that the future of his declining movement lay in this South American “Garden of Eden”.

Demands for fairer distribution of land are not unusual in Paraguay: most of it is owned by a tiny fraction of the population. The bill in Congress proposes seizing less than a tenth of the 600,000 hectares (1.5m acres) the Moonies own around Puerto Casado, for which they should get compensation—assuming the government can scrape together the money.

Though small in scale, the proposed seizure has caused a huge fuss. Paraguay's business federation laments that the country will never attract foreign investors if it mistreats the few, such as the Moonies, that it already has. The bill's congressional backers talk darkly of Mr Moon trying to build a “state within a state”.

Puerto Casado may be just another of Mr Moon's over-ambitious South American money-spinning ventures. Directly across the river in Brazil, his plans to build a model town, with new roads, hotels and classrooms, have had similarly underwhelming results. Late last year, Brazil's Movement of Landless Rural Workers led a mass invasion, claiming much of the project's land was lying idle. A bank bought by Mr Moon in Uruguay went into liquidation and his plans to redevelop a port there have been stymied by local opposition. For a would-be messiah, not much sign of miracle-working.

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Jamaica's crime wave

Calling Scotland Yard

Aug 11th 2005 | PORT OF SPAIN
From The Economist print edition

A silver medallist in homicide

"MI FATHER dead," wails a three-year-old girl, mourning one of at least 21 people killed since April in a war between gangs in the Balcombe Drive area of Jamaica's capital, Kingston. Besides being terrified of the gangs, locals are increasingly angry with the island's police, whom they accuse of idling while the gunmen run rampant.

Murder is the leading cause of death for Jamaica's working-age males and the appalling rate of killings has worsened sharply this year. Up to August 9th there were 1,028 murders, 25% more than in the same period last year. Though comparing national murder rates is fraught with problems, a United Nations study put Jamaica fourth behind Swaziland, Colombia and South Africa in 2000. If things go on as they are, Jamaica may soon have the dubious distinction of being at least the world's silver medallist in homicide.

Cocaine arrives in Jamaica by speedboat, from where it is sent to America and Britain. The drugs money fuels the gangs, whose tentacles reach into local politics. In the Grant's Pen district of the capital, for instance, one gang backs the governing People's National Party while its rival supports the opposition Labour Party.

Police corruption is a serious worry. The commissioner, Lucius Thomas, has admitted that bent cops traffic in guns and drugs. More than 60 have been suspended or sacked over various offences this year.

An alarmingly high proportion of Jamaica's shootings are by the police themselves. Eight police, including the high-profile former head of a disbanded "crime management" unit, will soon go on trial, charged over the deaths of four civilians in 2003. Carolyn Gomes of Jamaicans for Justice, a pressure group, says she has heard of nine new police killings in the past three weeks, which she cannot investigate, as "the police have locked off information".

Acknowledging that it needs outside help, in March Jamaica brought in Mark Shields, a top policeman from London's Scotland Yard, with experience ranging from organised crime to counter-terrorism. He will shortly be joined by four other senior crime-busters, who are currently being sought from the police forces of Britain, America, Australia and Canada.

Britain is especially keen to help, given the bloodshed that members of Jamaican drugs gangs sometimes cause on the streets of its cities. Britain's diplomatic mission in Kingston is its second-largest in the Americas and most of its 125 staff have at least some crime-related duties.

Though the death toll keeps rising, there has been some recent progress. Operation Kingfish, a carefully chosen police and army unit launched last October, has with international help seized 10 tonnes of cocaine and made arrests in Montego Bay, a centre for both tourism and drug-trans-shipment. Surveillance equipment has cut the flow of drug-carrying "mules". New patrol boats will soon arrive to chase the smugglers. New technology for fingerprinting and ballistics and new laws on using wiretap evidence may secure convictions in cases where witnesses run scared.

Optimists say the surge in gang shootings shows how the police are winning the drugs war, forcing the gangs to fight over shrinking spoils. But Jamaicans are deeply cynical about their police. They will rightly take a lot of convincing.

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MIDDLE EAST AND AFRICA
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African migration

Home, sweet home—for some

Aug 11th 2005 | JOHANNESBURG
From The Economist print edition

How can Africa move from brain drain to brain gain?

FOR Francois Pienaar, the World-Cup-winning former rugby captain, moving back to South Africa from England in 2002 was one of the best decisions he ever took. Going to Europe for a few years was a good professional move, but he missed friends and family and thought South Africa a better place to raise children. He has now become the poster boy for the Homecoming Revolution, a non-profit outfit helping South Africans living abroad to come back. Its aim, with a warning that it is not for "pessimists, racists, bigots and moaners", is to bring talent back home. Apartheid deprived the black majority of high-quality education, leaving the country with a shortage of skills that the education system is now struggling to remedy. The brain drain of the most highly qualified has worsened the problem.

Though hardly new, emigration accelerated after the country moved to democracy in 1994 and its international isolation ended. While 70,000 South Africans are thought to have left the country in 1989-92, the estimated number ballooned to over 166,000 in 1998-2001. Some 1.4m South Africans are thought to be living in Britain alone. According to official statistics, over 16,000 highly-skilled South Africans emigrated between 1994 and 2001, but the real numbers are probably three to four times higher. Close to half of the South Africans living in rich countries have higher-education degrees.

Official statistics do not offer a racial breakdown of migration, but a survey has indicated that white professionals are only slightly more likely to consider emigrating than black professionals. Whites probably make up the majority of those who leave, largely because they are disproportionately well-educated: close to 45% of South Africans with a university degree (and possibly over 70% of those with a doctorate) are white, though they make up less than 10% of the population.

But South Africa is hardly alone. The International Organisation for Migration (IOM) in Geneva reckons that the global stock of international migrants more than doubled in 30 years to 175m in 2000 and the African continent probably has the most mobile population in the world. Many Africans are pushed out by conflict or poverty. Those with exportable skills are lured by countries that pay better and offer more attractive career prospects, work conditions or lifestyle. South African expatriates also cite crime as a reason to leave, while some whites say that affirmative action to advance blacks is shrinking their career opportunities at home.

The effect of emigration is hard to assess. According to the Human Science Research Council, a South African think-tank, the country's research-and-development activity has been resilient. But the

departure of doctors and nurses, for instance, is hitting the region hard. The *British Medical Journal* has reported that 23,000 of them leave Africa every year. According to some estimates, 10% of hospital doctors in Canada are South Africans, while the countries whose nurses got the most British work permits in 2001 were South Africa and Zimbabwe. The IOM says that more Ethiopian doctors are practising in Chicago than in Ethiopia.

Emigration is aggravating already crippling staff shortages in many of Africa's state clinics and hospitals. Only 50 of the 600-odd doctors trained in Zambia since independence have stayed. In South Africa, over a quarter of annual vacancies for doctors and nurses in the state hospitals and clinics are unfilled; as many as two-thirds of such jobs outside the bigger cities are not taken up. About $1 billion has been spent on training South African health-care professionals now working abroad.

You can leave and still help

Those who leave can still, however, help their home countries develop. An increasing number of diaspora networks, such as the South African Network of Skills Abroad or the IOM's Migration for Development in Africa, are trying to foster research and exchange programmes or even business links between those who have left and those who have stayed. The Francophone Initiatives of African Women in France and Europe, another diaspora network, has contributed to humanitarian aid, vocational training for orphans and micro-credit for women in places like Congo, Gabon and Cameroon. Many African expatriates also send money back to their families. The amount is a lot higher than the $4 billion officially recorded in 2002, as cash often travels in suitcases or through informal channels. For small countries, such as Cape Verde and Lesotho, remittances make up 12.5% and 26% of GDP, respectively.

In a regional powerhouse like South Africa, the migration door swings both ways. The number of foreign students enrolled in South African universities, most of whom are from other African countries, is reckoned to have grown from 12,600 in 1994 to 35,000 in 2001. South Africa has also signed agreements with several countries, including Cuba and Germany, to lure doctors to South Africa for a specific period. New immigration rules, in force since last month, are supposed to make it easier for educated foreigners to move south, while staunching the inflow of illegal migrants; some 2m Zimbabweans are now said to be in South Africa.

Most African countries are still a long way from being tempting places to come back to. But those such as South Africa, with strong and sophisticated economies and fine amenities, are plainly better placed. South Africa The Good News, an outfit which has produced a series of books, arranges public events and has a website, all born out of the frustration of two Johannesburg businessmen tired of hearing their compatriots moan about their country, is trying to change perceptions. A lot of young South Africans working abroad are keeping their options open—and may come back. The Homecoming Revolution has organised events in London to convince South Africans that, in the wake of Mr Pienaar, it is worth returning. But it will be an uphill task.

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Kenya

The corruption is sickening

Aug 11th 2005 | NAIROBI
From The Economist print edition

And Britain raises hackles by saying so

Get article background

SINCE Mwai Kibaki won the presidency over two years ago, the subject of corruption has never been far away. In a decisive electoral reaction against the culture of graft and bribery that came to permeate every level of Kenyan society under his predecessor, Daniel arap Moi, Mr Kibaki won his mandate on an anti-corruption platform. The president has been cheered along by many Kenyans, fed up with the way their country's economic promise has been squandered by greedy politicians. Foreign donors are exhausted by the cynicism of those same politicians embezzling or misspending foreign aid.

But in the absence of any obvious sense of urgency from Kenya's own politicians, it is the donors, and particularly the British, the former colonial masters, who have made most of the running. Last month the British ratcheted up the pressure on Kenya's government by taking the aggressive step of banning a minister, Chris Murungaru, from visiting Britain. The move has caused a storm in Kenya and a lot of undiplomatic language about neo-imperialism and bullying. Relations between Kenya and Britain, one of its biggest donors, are at their lowest ebb for years.

The British government has refused to say why it has banned Mr Murungaru, but it is clear that allegations of corruption are at the nub of the row. For his part, Mr Murungaru says he is the victim of a personal campaign to discredit him waged by Britain, in particular by its recently departed high commissioner, Sir Edward Clay. It was he who made the most undiplomatic speech, in July 2004, when he condemned Kenya's corrupt government officials' “arrogance and greed” and “gluttony”, which caused them to “vomit all over the shoes” of donors. Earlier this year Sir Edward rammed the point home by handing Mr Kibaki a dossier of 20 “suspicious transactions”. The British Foreign Office has not confirmed whether Mr Murungaru has been linked to any of them, but notes that 18 of the cases are under investigation by Kenya's Anti-Corruption Commission.

What made Sir Edward speak out was a rising sense of despair among Kenyans and donors at the failure of Mr Kibaki's government to match words with deeds. Few doubt the president's integrity. In Mr Murungaru's case, the British note that Mr Kibaki himself has not joined the chorus of wounded pride that has filled the Kenyan press on the transport minister's behalf. Still, it is clear that the campaign against corruption has drifted since Mr Kibaki took over, especially since the government's top anti-corruption official, John Githongo, resigned earlier this year in frustration at his inability to pursue cases to the upper echelons of government.

It is impossible to measure corruption precisely, but Transparency International, a Berlin-based lobby, still rates Kenya as one of the world's most corrupt countries, on a par with Angola, Iraq and the Democratic Republic of Congo. The lobby's latest Kenya Bribery Index suggests that the number of bribery cases reported by the public in dealings between public and private officials has dipped from 40% to 34% of all encounters. But the average bribe paid has soared, from 1,484 Kenyan shillings ($20) to 4,958 ($68).

Kenya's tragedy is that, as East Africa's biggest and most sophisticated economy, it would be doing so much better—were it not for corruption. A prominent western banker based in Kenya calls it “a middle-income country performing as a low-income one”. Aaron Ringera, a judge who heads the Anti-Corruption Commission, says beating corruption is “a matter of life and death to this country”.

With Mr Githongo gone, many Kenyans see Mr Ringera as their last hope. He has brought several new bills before parliament to open up procurement practices and publish the financial records of ministers and members of parliament. He now claims to have all the legal weapons he needs and a team of 200 investigators. He also says he has several investigations into politicians' malpractice under way.

But to Mr Ringera's dismay, MPs will still not give his office the power to prosecute those cases; that remains the job of the attorney-general, who is a political appointee. Kenyans and donors will be watching closely what happens in those cases. By keeping corruption high on the news agenda, Britain may make Mr Ringera's job a little easier.

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Ethiopia

Hoping that a star won't fizzle

Aug 11th 2005 | ADDIS ABABA
From The Economist print edition

The West wants one of its favourite beneficiaries to stay virtuous

ALREADY at least 75m-strong, making it the second most populous country in Africa after 130m-strong Nigeria, Ethiopia could, by some estimates, be home to 140m people by 2030. It is not standing still: food production has more than doubled since 1993. Even so, by the government's own reckoning, 9m Ethiopians now depend on food aid and another 18m are malnourished. And as parts of the country become hungrier, ethnic divisions are sharpening. Demography is just one reason why Ethiopia's foreign well-wishers, who keep the economy afloat, are again getting nervous.

As food gets scarcer again, small bands of guerrillas in the south and east, most of them no more than cattle rustlers and displaced people, could turn local tensions into insurrections. There are worries, too, that a row over the disputed border with Eritrea, to the north, could flare up again into war, as it did in 1998 at a cost of 70,000 lives. The stability of the entire Horn of Africa, which is awash with cheap weapons, depends to a large extent on sensible governance in Addis Ababa, Ethiopia's capital. The burgeoning birthrate is just one of a number of reasons for worry.

More recently, the country's harmony has been threatened by political strife. A general election on May 15th was meant to mark the safe passage of Ethiopia from blood-soaked Marxist rule to multi-party democracy. The ruling Ethiopian People's Revolutionary Democratic Front, which toppled the Marxists in 1991 and has institutionalised power for itself since, has, according to Ethiopia's election board, won an outright majority of seats, though opposition parties did far better than before.

But the final results are still in dispute. The election board, stacked with Democratic Front sympathisers, has picked through a slew of ballot-rigging accusations and other abuses, including the beating and murder of witnesses to election fraud, mainly filed by two large opposition parties, the Coalition for Unity and Democracy and the United Ethiopian Democratic Forces. Their supporters took to the streets of Addis Ababa and other towns after the poll. On June 8th, police and troops fired on protesters who, they said, had been throwing stones, and killed some 40 of them.

Sorry isn't enough

The prime minister, Meles Zenawi, declared himself shocked and ordered an independent investigation; just how independent remains to be seen. Mr Zenawi's polished reputation abroad, for instance as a member of Tony Blair's Commission for Africa, will be badly damaged if he is found to have given the orders that led to the killing or to have had the ballot rigged.

The case of a military helicopter crew who defected to neighbouring Djibouti with its helicopter gunship is murkier still. By some accounts, it fled after being given orders to strafe opposition supporters. Two of the crew have apparently been bundled back out of Djibouti by Ethiopian intelligence to face charges.

The United States and the European Union's countries, which together provide Ethiopia with nearly a third of its budget, have urged restraint. A state of emergency enforced after the killings helped calm things down; it was lifted late last month. The hope is that the opposition will now take up its seats in the parliament. So far, the election board has given Mr Zenawi's lot 296 seats in the 547-seat parliament and called for a fresh vote in 31 constituencies on August 21st. The opposition, for its part, rejects the result in 299 constituencies.

Big ideological differences persist. The government wants continued state ownership of land, and federalism along ethnic and linguistic lines. The opposition wants some land privatised and thinks ethnic federalism undermines the state. On both scores, Mr Zenawi is likely to get his way.

But the picture is not simple. Though the government has an authoritarian undertow and there are complaints about shady deals, most recently over land sales in Addis Ababa, it has made progress on agriculture and roads, which together account for half Ethiopia's budget. And the opposition is hardly a paragon of virtue. Weak and muddled in its message, it has no talismanic figure to rally behind.

Foreign election observers are keeping their eyes open. If they find the election board to have been reasonably impartial and if Mr Zenawi proffers an olive branch, for instance by letting the new opposition-backed mayor of Addis Ababa have strong powers, foreign well-wishers will breathe a sigh of relief that one of its star beneficiaries is still, more or less, on the right road.

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Iran's nuclear programme

Are negotiations over?

Aug 11th 2005
From The Economist print edition

Iran's ruling mullahs may have crossed a point of diplomatic no-return

Reuters

Not a barrel of laughs

Get article background

IN THE saga of the West's efforts to prevent Iran from making a nuclear bomb, time just about ran out this week for an arrangement that might have satisfied all sides. The mullahs, who seem bent on acquiring technology which they insist would be for peaceful nuclear purposes only, summarily rejected as “insulting” a set of proposals from the three European countries (Britain, France and Germany, known as the E3) that have been negotiating, with American approval, on behalf of the European Union. Iran's new and ultra-conservative president, Mahmoud Ahmadinejad, reiterated his view that processing uranium was Iran's “right”.

Moreover, as a token of Iran's determination to press ahead with its nuclear plans, it symbolically broke the seals at a uranium plant in Isfahan where, among other places, it had promised to suspend its reprocessing activity while negotiations with the E3 were going on. As a result, the International Atomic Energy Agency (IAEA), the UN's nuclear watchdog, was feverishly trying to persuade Iran to think again.

But the die seemed cast. The IAEA's 35-country board held emergency meetings to decide whether to refer Iran's case to the UN Security Council, where, if the United States and the Europeans had their way, a resolution would be presented that would trigger punitive economic sanctions against Iran. It is likely but not certain that the agency's board will agree, in the next few weeks, to refer the case to the Security Council, though some non-aligned countries on the board, such as Malaysia and Brazil, sounded reluctant to do so.

More notably, however, Russia, which is building a nuclear plant for Iran but has agreed to ensure that the spent fuel that could be used for nefarious purposes will not kept by the Iranians, strongly criticised their decision. The swing vote, in the Security Council, might therefore be China, which has signed a number of big deals to buy Iranian oil and gas. Its ambassador to Austria, where the IAEA is based, appealed to Iran “to continue to apply the relevant confidence-building measures”—Chinese dip-speak for “don't do it”. It is conceivable, but still unlikely, that China would abstain in a sanctions-enabling vote in the Security Council.

The proposed E3 offer included trade incentives and security guarantees in return for an indefinite Iranian abstention from enriching uranium or separating plutonium as a prelude to creating a nuclear

fuel cycle that could be used to make bombs as well as nuclear power. The deal would also have endorsed Iran's role in regional security, with Iraq and Afghanistan both acknowledged as countries in which Iran has a legitimate interest.

But Iran wants more than that. Surrounded by countries that play host to American forces (Iraq and Afghanistan) or which already have nuclear weapons of their own (Russia and Pakistan), the mullahs seem determined, come what may (UN economic sanctions or, conceivably, a bunker-busting strike by a nuclear-armed Israel, whose existence Iran refuses to accept), to join the club.

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Japan

The lion's last roar?

Aug 11th 2005 | TOKYO
From The Economist print edition

Reuters

Japan's prime minister has launched a civil war with his own party, and called a snap election that could shake the country

Get article background

AFTER ruling Japan for most of the past half-century, the Liberal Democratic Party (LDP) tore itself apart this week over an issue that has come to epitomise the battle between its market-friendly reformists and its conservative old guard: the privatisation of Japan Post. On August 8th, in one of the most keenly watched votes in memory, the LDP's conservative wing mustered enough support in parliament's upper house to defeat the privatisation bills convincingly, by 125 to 108, with help from Japan's opposition parties. Junichiro Koizumi, since 2001 the LDP leader and prime minister, responded by making good his threat to call a snap election for the lower house (he cannot dissolve the upper chamber). Japan will go to the polls on September 11th.

The risks are huge: for Mr Koizumi, his party and for Japan. Although each of the two biggest contenders—Mr Koizumi's wing of the LDP and the opposition Democratic Party of Japan (DPJ)—backs a freer and more flexible Japan, neither may be able to win a clear majority. The immediate outcome could leave anti-reformists in a position of leverage, and perhaps greatly emboldened. For all the dangers, however, this could be just the moment for which many champions of real change have long been hoping.

Since he took over in 2001, Mr Koizumi has shaken up politics in many ways. Yet he has been unable to transform convincingly a system that routinely rewards caution and informal compromise over clear debate and crisp choices. Japan has thus been stuck in transition: between a one-party state in which LDP factions were the main contestants, and a modern democracy in which different parties compete. Now that the LDP is in turmoil, however, the September election could help to destroy the old system for good.

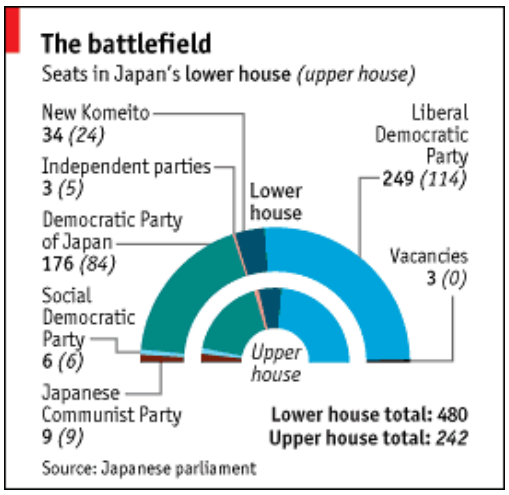
The DPJ is itching for a fight. After being formed in 1998 from a collection of splinter parties, it has gained seats and learned the ropes over the past few elections. Its leader, Katsuya Okada, said this week that the September showdown will be “the most important general election since the end of the second world war”. That is probably true.

The contest should be close. The LDP will withhold support from the 37 lower-house party members who

rejected the Japan Post privatisation bills when that chamber voted on them last month. So the LDP and its coalition partner, New Komeito, will be defending only 246 seats in the election, a bare five more than they need for a majority. And although opinion polls gave Mr Koizumi a boost this week, it is far from clear at the outset how the LDP split will affect its traditional strength in rural areas, or the DPJ's edge in the cities.

Foreign policy will be a factor. The DPJ will pledge to get Japanese troops out of Iraq. And many moderates and businessmen will back the DPJ in hopes that it will cool tensions with China and South Korea. Mr Koizumi has infuriated neighbours by going every year to the Yasukuni shrine, an institution widely associated with an unapologetic view of the second world war.

The economy, though, will help Mr Koizumi. He will claim that the latest rebound is due to his previous reforms: privatising road corporations, fixing the banks, cutting public-works spending and freeing up market forces in general. In fact, exports and investment, notably involving China, have played a much bigger role. This has boosted company profits and made it easier for the banks to write off bad loans. Mr Koizumi's government deserves credit for seizing the chance and pressuring the banks, but most of his other economic reforms have been gradual or weak.



Growth, though, is picking up. Hopefully, this will keep translating into more hiring, and eventually lead to rising wages, higher consumer confidence and an end to deflation. Despite all the political turmoil this week, the stockmarket rose by 5.3% between mid-day Monday (just before the upper house voted) and Thursday afternoon—closing at a four-year high.

The danger for Mr Koizumi is that by stressing one issue—Japan Post, which he has yet to explain clearly—he may fail to connect with many reformist voters. A majority of Japanese seem to agree with him about the need to separate the state from the postal system's ¥331 trillion ($3 trillion) stockpile of savings and life-insurance assets. But the DPJ will ask why the prime minister is so fixated on this one reform. By contrast, the DPJ is stressing how much it wants change on a range of fronts. Its members voted against the Japan Post privatisation, but they say they are only opposed to the details, not to privatisation in principle. The party will also hope that voters understand why the long-suffering opposition wanted to defeat the bills and trigger an election.

Mr Okada thus faces a different challenge: convincing voters that his party can carry out the changes they are promising, when they have never been in power before. The party manifesto pledges to shift power and finance towards regional governments; to unify a balkanised pension system to make it fairer and simpler; to cut back even more than Mr Koizumi has on public works and other sources of corruption; and to shrink the state. It is also offering goodies, such as more police, schools and nursing homes and the scrapping of tolls on public highways.

One criticism of the DPJ is that it is fragmented, just like the LDP. Its members include former liberals and LDP members, as well as former socialists. The manifesto, which all candidates must sign, is its way of promising cohesion. If it does win, the DPJ's internal differences will probably not be as big a problem, at least initially, as will the upper house, in which it will still hold a minority of seats.

Whatever the outcome, the split within the LDP is a huge event. Mr Koizumi took office in 2001 promising to “change the LDP, change Japan”. He is closer than ever to fulfilling the first half of his pledge.

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North Korea

Now what?

Aug 11th 2005 | BEIJING
From The Economist print edition

Six parties, 13 days, but no deal

Reuters

See you in three weeks

Get article background

FOR the fourth time since 2003, negotiators from six countries have been meeting in Beijing, seeking a deal that would end North Korea's nuclear-weapons programme. Now, for the fourth time, they have broken off with little to show in the way of results. While this round, which ended on August 7th after 13 hard-slogging days, produced some faint indication that small steps forward may be possible, the core issues seem as intractable as ever.

A draft statement circulated by China, the host, inspired the most substantial discussions to date. The parties—China, North Korea, South Korea, Russia, Japan and America—failed to endorse it, but they did end on a somewhat encouraging note. Rather than breaking off entirely as in the past, they called a three-week “recess”, and agreed to resume talks during the week of August 29th. Instead of being a sign of failure, this may mark a sincere effort calmly to take stock, and relieve the immediate pressure over the next set of moves.

More encouraging still, the main contenders, America and North Korea, did two things that have eluded them in the past. Despite George Bush's often stated refusal to deal bilaterally with North Korea, numerous bilateral sessions did indeed take place during the latest round, including a Korean supper. Just as important, both sides maintained a civil and business-like tone throughout, in sharp contrast with some of the name-calling that has gone before. Mr Bush once famously called North Korea's president a “pygmy”, and more recently a tyrant. North Korea has branded Mr Bush a philistine and a world dictator. Indeed, it was only after Mr Bush finally uttered a more polite public reference to “Mr Kim Jong Il” that North Korea agreed to revive the talks at all, after having stayed away for more than a year.

Given the issues at hand, politeness will only carry things so far. Big obstacles remain, and diplomats privately acknowledge the long odds against surmounting them. One is North Korea's insistence that it must retain a civilian nuclear capability, and America's refusal to allow that. “If the US really wants to make substantial progress in the Korean peninsula's nuclear issue, it had better make up its mind to change its policy,” North Korea's chief negotiator, vice foreign minister Kim Kye Gwan, said after the talks broke off.

Despite the improved tone, little trust exists between Washington and Pyongyang. Neither side thinks the other lived up to its commitments under an agreement reached to resolve an earlier crisis in 1994, itself the product of gruelling and protracted negotiations. America did not extend diplomatic recognition to North Korea as called for, and the promised light-water nuclear reactors were not built. More egregiously, say the Americans, North Korea initiated a covert uranium-enrichment programme.

North Korea has moved maddeningly between acknowledging and denying that programme's existence, but it is widely assumed that it does exist, and this poses another impediment to success in the six-party process. John Pike, director of GlobalSecurity.org, a think-tank, says that America has no idea about the size or location of this uranium programme, and is unlikely to win the intrusive, unfettered access to people and places that it would need in order to verify any agreement to abandon it.

For the moment North Korea appears willing to entertain offers from America (and South Korea) of food assistance, energy aid and security guarantees in exchange for denuclearising. However, it may well conclude that a credible nuclear threat provides its only real means of deterring a potential American attack—which, no matter how often America promises it has no plans for one, it evidently fears. That calculation might survive any number of talks.

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South Korea

Free speech and witch hunts

Aug 11th 2005
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A train, a dog and a backlash against growing "cyber violence"

EARLIER this year, the photograph of a young South Korean woman who failed to clean up after her dog in a railway carriage appeared on the internet. Web-users throughout the country co-operated to reveal her identity, and for weeks the woman, quickly dubbed the "dogshit girl", became the number one hate figure among the country's cyber community. Vicious and defamatory messages appeared on the internet and her university website was bombarded with hate mail.

Such cases of "cyber violence" are reaching alarming proportions in South Korea, prompting a shift in public attitudes towards the exercise of unbridled free speech on the web. In the early days of the dog incident, bloggers were unconditionally critical of the woman's anti-social behaviour. Now, criticism has been replaced by growing concern about witch-hunts.

South Korea has the highest rate of broadband penetration in the world. This, together with the tightly knit nature of Korean society, has given these cyber-attacks a brutal edge. The victims of digital persecution range from the female Korean singer who was forced to deny wild and unsubstantiated rumours that she was a man to the schoolgirls whose photos and personal details were splashed on the net after allegedly driving a classmate to suicide.

The speed of technological change, as well as the cases of attacks meted out over the internet, has left the authorities struggling to respond. The government has said that freedom of expression must be balanced with responsibility as it considers measures to crack down on harassment over the web. One proposal would require Korean web users to register their personal information before leaving messages on bulletin boards—a measure supported by the vast majority of citizens, according to a recent government-backed online survey.

However, critics of the "real-names system" oppose the plan, saying it undermines the freewheeling nature of the internet and would suppress legitimate criticism and minority opinions. They also question its feasibility. The canine incident has sparked public debate, but that will be of cold comfort to the woman involved, whose reputation has been annihilated. She has reportedly been forced to drop out of university.

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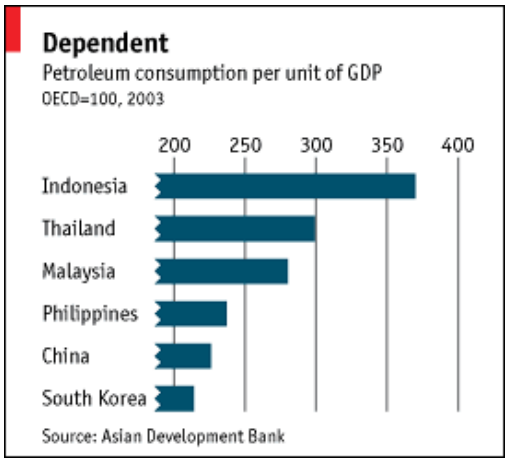
South-East Asian and oil

The black and blue stuff

Aug 11th 2005 | BANGKOK
From The Economist print edition

Producers and consumers alike are hit



LAST year, while trying to predict the effect of high oil prices on the economies of South-East Asia, the Asian Development Bank (ADB) came up with three scenarios. In the gloomiest of the three, the oil price was projected to hover at around $40 a barrel throughout 2005—enough, the bank predicted, to knock over two percentage points off the growth rate in several countries. The reality, however, has proved considerably bleaker. In the first seven months of the year, the oil price averaged over $50 a barrel, with no respite in sight. The toll on the region's economies is much as the ADB foresaw.

Developing countries tend to consume more oil per unit of output than rich ones, and so suffer more from high oil prices. South-East Asia is no exception: Indonesia, Malaysia, the Philippines and Thailand all consume between two and four times more oil than the average for rich countries. No wonder inflation is ticking up across the region, albeit from historic lows in several countries. Central banks have begun to raise interest rates accordingly, despite faltering growth. The Bank of Thailand, for example, has raised interest rates six times in the past year. Meanwhile, it has gradually lowered its forecast of Thailand's economic growth this year, from 6% in January to 4% now. In the first quarter of the year, the economy actually shrank slightly compared with the quarter before.

For countries that are obliged to buy most of their oil abroad, the high price is also pushing up imports, and so taking a toll on the balance of trade. That, in turn, puts downward pressure on local currencies, making oil imports all the more expensive. Once again, Thailand has been hardest hit: in the first quarter, it posted a current-account deficit for the first time since the Asian financial crisis of 1997-98.

The Philippines has also seen its import bill rise, as has Indonesia, which became a net importer of oil in 2003, despite being the region's only member of the Organisation of Petroleum Exporting Countries. Indeed, when Pertamina, Indonesia's state-owned oil company, ran low on stocks last month, and so began buying up dollars to pay for imports, the rupiah plunged. Even for Malaysia, the region's biggest exporter, the high oil price is not necessarily beneficial. According to the ADB's models, at $40 a barrel the benefit of higher oil revenues is outweighed by the reduction in demand for the country's other exports as the world economy slows.

Governments around the region have responded with all manner of half-baked energy-saving measures. Government offices are to be less strongly air-conditioned, billboards and some street lights are to be turned off during the wee hours after midnight, and so on. The Thai government has curtailed the

opening hours of shopping malls. The authorities in Indonesia ordered television stations to go off the air at night, although they subsequently exempted broadcasts of European football matches, to which many of their compatriots are addicted. Civil servants in the Philippines have been put on a four-day working week, to save the petrol they use while commuting and the power they consume in their offices.

But the region's politicians have been slow to take the most obvious step, of cutting fuel subsidies. Last month, Thailand eliminated subsidies on diesel, a scheme that had cost it some $2 billion over the previous 18 months. The government of Malaysia, for its part, raised fuel prices for the fourth time in the past year on July 31st, reducing, but not eliminating, its subsidies.

The biggest laggard is Indonesia. Last year, its bill for oil subsidies ballooned from 14 trillion rupiah ($1.75 billion) to 72 trillion as the underlying oil price rose. After much deliberation, it eventually raised fuel prices in March by roughly 30%, in an attempt to shift spending to more useful outlets, while promising voters not to raise prices again this year. Since then, however, the continued rise in the oil price has meant that the cost of fuel subsidies has actually risen. The government is now likely to spend as much as 100 trillion rupiah on the subsidies—or twice as much as it has budgeted to rebuild the tsunami-stricken province of Aceh.

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Laos

Vicious triangle

Aug 11th 2005 | VIENTIANE
From The Economist print edition

An opium ban is a mixed blessing

Get article background

IN A rush to comply with its promise to eradicate poppy cultivation this year, Laos last month proclaimed itself opium-free. It is not, but a survey by the UN's drugs unit has confirmed that there has been a very substantial reduction in opium production, bringing it to about a quarter of its level in 1998. Antonio Maria Costa, head of the UN Office on Drugs and Crime, even forecasts that the end of the infamous “Golden Triangle” could be in sight—if present progress can be sustained. That is a big if, though.

Mounting evidence of the drug war's casualties is meanwhile starting to emerge, to the embarrassment of both donors and the Laos authorities. More than 65,000 Akha, Hmong and other Laotian hill-dwelling tribespeople, for whom opium production is the main livelihood, have been cajoled and coerced to abandon the crop. Now they are dying from disease and malnutrition in the resettlement villages to which many have moved.

Charles Alton, a consultant for the UN Development Programme, reported in 2004 that hill-tribe people moving to new villages were not only short of rice but also faced diseases—malaria, gastro-intestinal problems and parasites—that were seldom experienced up in the mountains. An international NGO has documented mortality rates among such people at almost four times the national average.

The Laotian government long tolerated opium cultivation, in the absence of alternative livelihoods. But since 2000, increased pressure from America and the EU has persuaded it to take a tougher line, as has the promise of millions of dollars of extra aid money.

Laotian opium—about 100 tonnes a year in the 1990s—has only ever made a marginal contribution to the global drugs trade; Laos has never been in the same league as Afghanistan and Myanmar. Moreover, few Laotians have traditionally been addicted to the stuff. Besides being a cash crop, it is used as medicine and, as part of tribal culture, smoked on special occasions. Yet, perversely, the victory over opium production has triggered worsening drug abuse.

One leading Laotian researcher says that, for lack of opium, people are turning to far more dangerous

drugs such as heroin and *yaaba* (amphetamines), which flood across the Burmese border. Another critic, David Feingold, an anthropologist, says that the opium-eradication programme is ill conceived and badly executed. He predicts that increasing heroin use, and the impoverishment of highland women, which increases their vulnerability to trafficking, will assist the spread of AIDS.

In response to such humanitarian concerns, Mr Costa of the UN's drugs office has appealed for more international aid to compensate the tribespeople for their loss of opium income. But aid workers in Laos query how long such a policy can be sustained, given that alternative crops often provide miserly returns from uncertain markets, not least because of Laos's appalling infrastructure. One says that the hill-tribes will always go back to opium, “unless the government uses repression to stop them”.

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India

Delayed reaction

Aug 11th 2005 | DELHI
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A massacre in 1984 brings a ministerial resignation at last

Get article background

AFP

Still angry after 21 years

"A BLOT on the nation's conscience," said India's prime minister Manmohan Singh in parliament on August 10th, referring to the 1984 slaughter of his fellow Sikhs in Delhi. The "national shame" lay not just in the orgy of thuggery, arson and murder that followed the assassination of Indira Gandhi, then the prime minister, by her Sikh bodyguards and left perhaps 3,000 people dead. It lay also in the failure to punish any of the culprits. Later that day, in a hint that the wheels of justice may at last begin to turn, Jagdish Tytler, the minister in Mr Singh's government responsible for overseas Indians' affairs, felt forced to resign because of accusations about his role in the riots.

These had been repeated in the report of the latest—ninth—commission to inquire into the riots. Tabled in parliament on August 8th, it had cited "credible evidence" against Mr Tytler and a number of other figures in the ruling Congress party. Mr Tytler, it said, was "very probably" involved in organising the riots. One affidavit signed in 1987 by a young Sikh claiming to be an eyewitness quoted him: "I had promised large-scale killing of the Sikhs."

Mr Tytler protests his innocence, and the government argued there was not enough evidence for legal action against him or the others. Both the main opposition party, the Bharatiya Janata Party, and Congress's allies, the Communist parties, said that heads should roll. Congress pointed out the hypocrisy of the BJP's position. Unlike Mr Tytler, its leader, L.K. Advani, faces legal charges for allegedly inciting the riot that led to the demolition of a mosque in Ayodhya in 1992, and to vicious communal violence thereafter. More recently, in 2002, the BJP-led government in the state of Gujarat was accused of complicity in an anti-Muslim pogrom that killed perhaps 2,000 people. There, too, not a single murderer has been convicted.

Congress, which is now led by Mrs Gandhi's daughter-in-law, Sonia, is proud of its "secular" tradition—she, after all, was born Italian and forsook the prime minister's post in favour of a Sikh. But many Sikhs were not satisfied by Mr Tytler's resignation and that of his party colleague, Sajjan Kumar, from a post in the Delhi local government. They would like to see killers punished, and would have respected Congress much more if its action against Mr Tytler had been spontaneous, rather than a surrender to political pressure.

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Internet business strategy

Yahoo!'s personality crisis

Aug 11th 2005 | SAN FRANCISCO
From The Economist print edition

Yahoo! is doing so many different things that it may have neglected to figure out what it wants to be

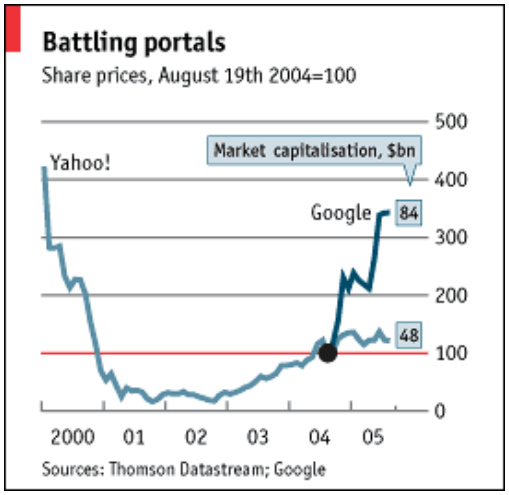
Get article background

STUDENTS from Harvard Business School and MIT's Sloan School of Management were recently invited to play a “war game” between the big four internet portals—Yahoo!, Google, Time Warner's AOL, and Microsoft's MSN. The organiser, Fuld & Company, a consultancy, split the students into teams, which began by delivering a brutally honest analysis of each firm's position and then did battle. Yahoo!, its team thought, is in essence a smorgasbord. “I don't have to be the best at everything; I just have to be good enough for you,” said the team's presenter. Google's team, by contrast, was confident that it alone was the true technological innovator. The MSN team, predictably, talked mostly about “leveraging Windows”, Microsoft's ubiquitous operating system, which excited nobody. And the AOL team began its presentation by saying that “we are fortunate just to be invited to the party.” In the end, Google won and Yahoo! came last. The winning team got $5,000.

In the real world, the stakes are far higher, but the basic analysis may prove correct. As if to prove the smorgasbord theory, Yahoo! this week finalised a $1 billion deal with Alibaba.com, a Chinese firm, that will give Yahoo! greater exposure to the promising, fashionable Chinese market, but may make Yahoo!'s product portfolio even less coherent. Yahoo! is primarily a consumer site, with everything from web search and web mail to news, music, photos, games and live chats. Alibaba has been mainly a business-to-business site that hooks up Chinese wholesalers and foreign retailers. This fits a pattern. Terry Semel, Yahoo!'s chief executive since 2001, has “done a notable job turning Yahoo! around” since the losses of the dotcom bust, says Jerry Michalski, a technology visionary in Berkeley, “but in the process he has turned it into, well, a bit of a tart.”

All things to all men

Yahoo!, of course, would disagree. “The only place anyone needs to go to find anything, communicate with anyone, or buy anything,” is how the firm describes itself, adding that it has a web audience of over 345m users in 25 countries. This appears to be paying off handsomely. Last month, Yahoo! reported quarterly revenues up by 51%, and profits up by 70%, compared with the same period last year (excluding the spectacular profits that Yahoo! made by selling shares it owned in its rival, Google). Internet advertising is growing fast, but Yahoo! is growing even faster, said Mr Semel.



Yet by other measures, Yahoo! is not the hottest thing on the internet. Microsoft appears to consider Google its only real threat, and vice versa. If the standard is product excellence, Google seems to be the clear winner in the biggest category, search—its share of searches has been rising, to 52% in America as of June, whereas Yahoo!'s has fallen, to 25%. Ditto for music, blogging, pictures and many other categories—in each, there is another firm that most users currently consider better. If Wall Street is the judge, Yahoo! also loses—with roughly equal revenues, it is worth only 60% of Google's market capitalisation of $84 billion (see chart).

The question, then, is what Yahoo! is ultimately planning to become that is different from its rivals. One clue is the people it is hiring. Starting with Mr Semel, a Hollywood veteran and former technophobe, Yahoo! has been recruiting traditional media types. Its head office is in Silicon Valley, but Yahoo! has been expanding a campus in Los Angeles. Google has nothing in Hollywood, and is hiring software geeks, starting with its chief executive, Eric Schmidt, who previously ran Novell, a software firm, and was chief technologist at Sun Microsystems, a big hardware maker.

Google, in short, is at heart a technology firm. It is about algorithms. Yahoo! sees itself as a media firm. “Google says ‘trust the machine’; Yahoo! says ‘trust the editor or the community’,” says Paul Saffo of the Institute for the Future. “Its DNA is editors and making recommendations to other people.” Consider, say, the difference between the firms' news sites: Google's story list is picked by computers with no human intervention; Yahoo!'s is edited by journalists. Yahoo!'s Hollywood types do deals with film studios and news organisations—from September, for instance, Yahoo! will offer video feeds from ABC News and CNN. Google's geeks “merely” try to write great computer code.

Yahoo!'s ambition is to become the leader in the 21st century's media industry. In this era, it believes (with almost everyone in the internet industry), content will no longer be generated by a few large, wealthy firms, but by users themselves, through their photo and video blogs, podcasts, hyperlinks and so on. Hence Yahoo!'s purchase of Flickr, a site where people can share pictures with the public or their friends. And hence Yahoo! 360, a service, to be launched this summer, that lets users combine their photos and music, restaurant reviews and blogs in a personal space into which they can invite other Yahoo! users by instant-messaging, voice chatting or simply hyperlinking. Yahoo! wants to “marry search with community,” says Jeff Weiner, Yahoo!'s search boss.

There is a huge problem with this vision, however. Yahoo!'s “business model is necessarily in conflict,” says John Battelle, the author of a forthcoming book on the search industry. With so much content owned by Yahoo! or generated within its site by users, the quandary for the firm will be: “Do you point people to your own stuff or to the most relevant stuff?” If the former, Yahoo!'s reputation as a trusted internet search and navigation brand may evaporate; if the latter, its content may not earn the returns to justify Yahoo!'s investments in it. By contrast, says Mr Battelle, Google, which has chosen not to make content, does not face this conflict.

The dilemma may be even larger than that. “The Yahoo! guys are trying to create a walled-garden experience; they're like AOL in ’95,” says Tony Perkins, the founder of AlwaysOn, an online social network for technology insiders. That is not a compliment, as AOL, which began as a proprietary online service, started its long decline at about that time, after missing the impact of the new, open environment of the world wide web. With “closed” services like 360, says Mr Perkins, it is now Yahoo! that is missing the trend toward an ever more “open web” that will be “full of one-trick ponies” all

available at a single click. If Yahoo!'s users get the feeling that they are being ushered to sites purely because they belong to Yahoo!, reckons Mr Perkins, they will simply click out.

This may be Yahoo!'s fatal flaw. “MSN and AOL are going nowhere,” says Mr Saffo, for they have “no soul, no passion.” Yahoo! has passion, like Google and other newcomers. It may also have correctly spotted the shift from old media to new, user-generated media. But, says Mr Saffo, it seems to have missed one thing. The “world of the few and large” belongs to media in the 20th century, whereas this century will bring a “world of the many and small”. Yahoo!, in short, has old-media plans for the new-media era.

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China and the internet

Imperial bubble?

Aug 11th 2005 | HONG KONG
From The Economist print edition

A new Google clicks with investors

Get article background

CHINA'S leading internet search engine, Baidu.com, is named after a 900-year-old Song Dynasty love poem about the search for a beautiful woman. *Baidu*'s literal meaning—"hundreds of times"—represents the tortuous quest for the ideal. Baidu's owners, including (with a 22% stake) its chairman, Robin Li, did not have to work that hard to achieve financial bliss. Just five and a half years after founding Baidu, they listed it on America's NASDAQ exchange only to see the stock soar by 354% on its August 5th debut, the largest first-day gain since the dotcom bubble. At its closing price on that day of nearly $123 a share, up from the flotation price of $27, Baidu was worth nearly $4 billion, more than any other Chinese internet firm and almost 3,000 times last year's profit.

Naturally, the "Chinese Google", as it has been nicknamed, holds enormous promise. Its prospectus forecasts that the number of search-engine users in China will rise to 187m by 2007 from 115m today. And while China's current search-related advertising market is still small at $150m in 2004, according to Shanghai iResearch, Baidu has a juicy 45% of that. Certainly the real Google has performed beyond anyone's expectations, both as a business and as a share. At least some of the enthusiasm over Baidu's initial public offering stemmed from investors who missed out on the Google flotation and saw this as a second chance. The fact that Google also owns 2.6% of Baidu, and the news this week that America's Yahoo! will spend $1 billion on a stake in China's Alibaba (see article) adds the enticing prospect of consolidation. Perhaps the future holds a takeover by its bigger cousin, pitched at an even higher price.

Meanwhile, Baidu will have to compete with Google, already the second-biggest search engine in China. Unlike Google, in its main market Baidu faces an unpredictable government, determined to maintain strict control over the internet and the media in general. Its recent crackdown on the content of mobile-phone text messages, for example, hit the profits and shares of several Chinese online firms listed in America, including SMS provider Linktone and portals Sohu and NetEase. In all, the 23 mainland technology firms that have floated on NASDAQ since 2000 enjoyed a median first-day gain of 13% only to see their shares record a median decline of 34% one year on, according to Straszheim Global Advisors, a consultancy that focuses on China. With more Chinese firms preparing for overseas listings—such as A-Max Technology, which makes MP3 music players, China Medical Technologies, and Focus Media, which sells advertising space on liquid-crystal display screens—that should give foreign investors pause for thought. As the Song poets realised long ago, the achievement of perfection requires judgment as well as enthusiasm.

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Corporate governance in America

The rights and wrongs Ovitz

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From The Economist print edition

What the Disney verdict means for boards of directors

IF NOTHING else, the lawsuit concerning the hiring and firing of Michael Ovitz by the Walt Disney Company has ensured that corporate-governance can never again be dismissed as irredeemably boring. The trial, although concerning events at the media giant in 1995-96, commanded acres of space in the sorts of gossipy society magazines that had not hitherto been interested in the nuances of directors' fiduciary responsibilities to shareholders.

The trial, before Delaware's Court of Chancery, generated much colourful detail, most of it highly embarrassing to all concerned, especially Mr Ovitz and Disney's then chief executive, Michael Eisner, who fell out spectacularly with the longtime friend he had hired as his number two and ended up 14 months later paying a package worth $140m to go away.

However entertaining, the case did nothing for the Disney shareholders—and the usual bunch of class-action lawyers (see article)—who brought it. This week, a judge rejected their claims that members of Disney's board of directors breached their fiduciary duties to shareholders. This decision—especially given the overwhelming evidence produced in the trial that Disney's corporate governance was far below what would nowadays be considered adequate—was greeted with dismay by shareholder activists. That is unfair. In fact, the 174-page ruling, by Delaware's Chancellor, William Chandler, is full of common sense, and should be essential reading for anyone interested in good corporate governance.

Judge Chandler is clearly appalled by what passed for corporate governance at Disney in the mid-1990s. As he writes in one devastating paragraph:

> By virtue of his Machiavellian (and imperial) nature as CEO, and his control over Ovtiz's hiring in particular, Eisner to a large extent is responsible for the failings in process that infected and handicapped the board's decision-making abilities. Eisner stacked his (and I intentionally write “his” as opposed to “the company's”) board of directors with friends and other acquaintances who, though not necessarily beholden to him in a legal sense, were certainly more willing to accede to his wishes and support him unconditionally than truly independent directors.

As for the hiring of Mr Ovitz, on what was then possibly the highest package ever given to a non-boss, Judge Chandler concludes that “for the future, many lessons of what not to do can be learned from defendants' conduct here.” Given the importance of Delaware law to big American firms, most of which are incorporated there, expect those lessons to be widely learned. Indeed, this week's decision arguably means that directors will be legally liable in future if they do not learn them.

So why on earth were the defendants acquitted? Put simply, the judge distinguished between getting a decision wrong, and doing wrong—a crucial distinction that has sometimes seemed to be ignored during America's backlash against bosses in recent years. The decision to hire Mr Ovitz clearly turned out to be a poor one, such that firing him—even at a cost of $140m—was probably the right thing to do. But taking poor decisions is not by itself a breach of a director's, or an entire board's, fiduciary duty of care to shareholders. Under Delaware's “business judgment” rule, directors are protected if they can be shown to have followed proper procedures and done so in good faith. The worst that can be said of Disney's directors, concluded Judge Chandler, fairly convincingly, was that they did not act in bad faith, but may have been guilty of “ordinary negligence”—which, under the business judgment rule, is not enough to breach fiduciary responsibility.

There had been fears that a ruling against Disney's board would have been seen as a mortal blow to the business judgment rule, leading to a paralysing risk aversion in American boardrooms as directors

minimised their legal exposure. If so, said Judge Chandler, who clearly shared those fears: “The entire advantage of the risk-taking, innovative, wealth-creating engine that is the Delaware corporation would cease to exist, with disastrous results for shareholders and society alike.”

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German media companies

Profits and politics

Aug 11th 2005
From The Economist print edition

A controversial acquisition

Reuters

"TO BE in power in Germany, you need *Bild*, *Bild am Sonntag* and television." So Gerhard Schröder, now Germany's chancellor, once said, exaggerating only a little. One of the centre-left Social Democrat's disadvantages in his past pursuit of Germany's top political job was to have neither *Bild*, a newspaper with some 12m readers, nor its Sunday edition on his side. Both belong to Axel Springer, Germany's biggest newspaper publisher, which—as well as being pro-America and pro-Israel—has strong sympathies for the centre-right Christian Democrat Party.

Soon the left's problem may get worse. With the acquisition of ProSiebenSat.1, Germany's biggest private TV company, Springer is set to become a formidable force in television, too. As a result, there has been outrage on the German left, and among supporters of media pluralism, who want the merger to be blocked. Such concentration of power in print, television, advertising and the job market for journalists is very worrying, says Ludwig Stiegler, a Social Democrat MP.

As yet, none of Germany's top politicians have openly criticised the deal. "They are all too scared to pick a fight with *Bild*," says Siegfried Weischenberg, a professor of journalism at the University of Hamburg. *Bild*, on the other hand, is currently trying to appear less partisan. In recent weeks it has regularly published close-up pictures of the growing belly of Joschka Fischer, Mr Schröder's foreign minister, who is often struggling with punishing diets. Yet it has also made fun of the apparent lack of familiarity with basic economics of Angela Merkel, the Christian Democrats' candidate for chancellor.

The left can also take some comfort from the fact that Springer's takeover of ProSiebenSat.1 will be completed too late to influence Germany's national elections in September. The €4.2 billion ($5.2 billion) deal was announced on August 5th, but still requires the approval of the antitrust authorities, which may take until Christmas—assuming it is not blocked, as its critics hope but do not expect. Michael Konken of the German Association of Journalists concedes that, alas for him, the deal is likely to be permitted because the antitrust authorities look at the markets for print and TV separately. At about 30%, ProSiebenSat.1's share of the television market and that of Bertelsmann's rival RTL Group is roughly the same.

Concern about its new power as a media behemoth is dismissed by Springer as "hysteria" and the "reflexes of the 1968 generation"—a particular dislike of the chief executive of Springer, Mathias Döpfner (pictured), whom one rival German media executive dubs "Mr Neo-con". If all goes to plan, by June 2006 he hopes to merge the five TV channels owned by ProSiebenSat.1 and its 70 newspapers and 150 magazines into one conglomerate. This will create a sort of mini-version of Bertelsmann, Germany's biggest media group—a significant stride forward for Mr Döpfner, who has been described by someone who met him at dinner recently in New York as "a man of extraordinary ambition who wants to rule the world."

For over a year there have been rumours of talks between Mr Döpfner and the private-equity investors in a consortium led by Haim Saban, an American financier, that has controlled ProSiebenSat.1 since August 2003. Both firms have recovered from a recent crisis. Mr Döpfner, became chief executive in 2002 following Springer's first ever loss the previous year. By 2004 he had, despite a few years of sinking advertising revenue, delivered the firm's highest ever operating profit, of €336m. Last year's €217m pre-tax profit at ProSiebenSat.1 was also a record, reflecting its revival under Mr Saban.

Does the acquisition make good business sense? Springer has tried TV before, and failed. The deal will

weaken its strong balance sheet. The merged firms will remain dependent on the highly cyclical advertising market. Advertisements generate much of both firms' revenue.

Most analysts say that the merger will offer few synergies. The price is much too high and the timing is not good, says Peter-Thilo Hasler of HypoVereinsbank. The price implies 29 times estimated earnings per share for 2006. ProSiebenSat.1's profits have more than doubled since it was taken over by Mr Saban's consortium. They may not grow as fast in the future.

Past experience shows that cross-selling does not work for media conglomerates. Bertelsmann does not promote RTL's TV shows in its magazines more than those of ProSiebenSat.1 because that would lose readers, says Mr Hasler. Nor, he says, will offering advertisers a cross-media package do the trick either. The media-buying arms of advertising agencies are, alas, extremely efficient at negotiating such packages with print, TV and other media companies.

“So what?” retorts Springer. Its aim in becoming a media conglomerate is not synergies, but growth. It wants to add a second lucrative business to print. It says it knows that cross-selling in media is not very successful. “We also know that we don't know television,” says a Springer spokeswoman. That is why it is retaining the entire management team of ProSiebenSat.1, and why Mr Saban will continue to advise the company.

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European utilities

A very long engagement

Aug 11th 2005 | PARIS
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Suez and Electrabel wed at last

THIS was one of the longest courtships in corporate history. For over ten years Suez, a French water and power company, considered merging with Electrabel, a Belgian electricity firm. On August 9th Suez finally took the plunge, announcing its €11.2 billion ($14 billion) purchase of the 49.9% of Electrabel shares that it did not own.

In recent months, Suez had come under fierce pressure to either sell its stake in Electrabel or buy out minority shareholders. These calls came loudest from Eric Knight, of Knight Vinke Asset Management, an American investment firm, backed by CalPERS, an American pension fund and by Edouard Stern—until the controversial French banker was murdered in March. Mr Knight argued that Suez's partial ownership of the Belgian utility dragged down the shares of both firms. He filed suit in Brussels against both Suez and Electrabel, although he has now suspended his legal action following this week's deal.

As recently as May, Gérard Mestrallet, Suez's boss, had publicly dismissed Mr Knight's arguments. Yet his actions suggested he was preparing for a deal—not least by trying to reassure the Belgian public about the fate of a national champion that supplies 90% of Belgium's electricity. Last September, he replaced Willy Bosmans, head of Electrabel, with one of his confidants, Jean-Pierre Hansen—strikingly, Mr Hansen is also Belgian. Mr Mestrallet also pledged in a letter to the prime minister to increase the Belgian presence on the merged firm's board and to grow its Belgian operations.

After two years of painful restructuring, Suez can now probably afford careful expansion. In 2002-3, the firm made big losses and its debt soared. Mr Mestrallet has since slashed Suez's debt from €28 billion to €11.5 billion, by cutting costs and selling assets, and last year returned the firm to healthy profitability.

Analysts have mostly welcomed this week's deal. Electrabel was already Suez's most valuable asset. Last year, Electrabel contributed some €475m of Suez's total profits of €1.8 billion. Yet, without a full merger, Suez could not make use of Electrabel's balance sheet or its cash.

The Electrabel marriage solidifies Suez's new strategic emphasis on Europe. This has replaced an enthusiasm for emerging economies that often left it badly burnt. In Argentina, for instance, where in the 1990s Suez invested $1.7 billion in the private water industry, in 2002 the crisis-stricken government converted dollar-denominated prices into devalued pesos and froze tariffs despite sky-high inflation. In its ongoing battle with the Argentine government over tariffs and investment, on July 26th Suez threatened to leave the country if a solution is not found soon. This week Mr Mestrallet described his discussions with the Argentine government as still “extremely difficult”.

Mr Mestrallet says that one reason for now merging fully with Electrabel is the recent partial privatisation of Gaz de France and the coming partial privatisation of Electricité de France (EDF), probably in October. Suez wants to be ready to compete against Europe's power giants, RWE and E.ON of Germany and EDF. That ambition gives ammunition to shareholder activists in another campaign. They want Suez to split its water and power operations into separate firms because, they say, the two would be more efficient apart. This week Mr Knight vowed to continue his fight.

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Mining

Striking gold

Aug 11th 2005 | JOHANNESBURG
From The Economist print edition

A labour dispute hits South Africa's struggling gold mining industry

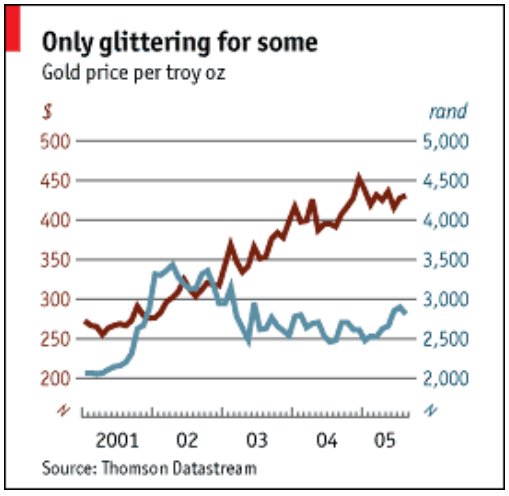
Get article background

AFP

FOR the first time in 18 years, South Africa's gold miners have laid down their tools. After wage negotiations failed, the National Union of Mineworkers began a strike on August 7th, joined a day later by Solidarity, a union representing skilled, mainly white, mine employees. Over 100,000 miners went on strike, halting the country's four main gold producers—AngloGold Ashanti, Harmony Gold, Gold Fields and South Deep—which together generate over 80% of the country's output. The strike costs 130m rand ($20m) a day in lost production. So far, this has not moved world gold prices, but, if it continues for long, it is likely to hit South Africa's already struggling gold industry quite hard.

Wages rose by 10% in 2003 and 7% last year, above headline inflation. But the unions say that the cost of living for their workers has grown faster than average prices. They also argue that a pay rise of a few percent does not amount to much on a minimum wage of 2,200 rand a month. They initially demanded a 12% rise, against the employers' offer of 5%—a gap that negotiations narrowed but failed to close.

This comes at a bad time for South Africa's gold mining industry—now less significant for the country's economy than platinum—which has seen its share of global output fall from 68% in 1970 to 14% today. Last year, South Africa produced less than 345 tonnes, the lowest since 1931.



As deposits thin, mining is taking place at ever greater depths—sometimes 4km (2.5 miles) underground—which has pushed up production costs, and made production more reliant on labour, which plays a bigger role at such depths. Hence the employers' reluctance to settle too high. Other costs have been rising, too, including for water, steel and transport. Even worse, the rand has more than doubled against the dollar since 2001, melting away dollar increases in the world gold price (see chart). In short, margins have been squeezed, and over half of the country's gold is now produced at a loss or just above break even. Slashing costs has become vital. The industry has shed around 30,000 workers

in the past two years.

Worse news may be to come. The South African government has held discussions with the mining industry about aligning royalties and taxation with international practice. This would eventually mean higher charges. On the other hand, there appears to be less cost than had been feared from a new law that transferred mineral ownership to the state, and gave mining firms five years to satisfy several obligations—including a transfer of capital into black hands, intended to correct economic inequalities inherited from apartheid—to keep their right to mine. Harmony and AngloGold Ashanti have each recently secured new mining rights.

Harmony, which has tiny margins and extracts 90% of its gold in South Africa, is expected to suffer most from the strike. Its operating profits have fallen by over half in the past year. It recently reported an overall annual net loss of 3.5 billion rand. AngloGold Ashanti, however, enjoys lower production costs and relies on South Africa for less than half of its output, and was the first to break ranks by offering workers an up to 6.5% salary increase. The other mining firms have now followed suit and improved their offer. As *The Economist* went to press, the miners were due to vote on the latest offer. As they are losing 60m rand in wages every day, there are powerful incentives for both sides to settle.

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The water industry in India

Private worries

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From The Economist print edition

Another setback for reform of India's water utilities

"MULTINATIONALS and profit sharks versus the people of India," is how one respected newspaper summed up a controversy surrounding Delhi's water board, the Delhi Jal Board (DJB). The row contains most of the elements that usually raise hackles among India's anti-globalisers. Alas, the ideological debate may delay a solution to Delhi's water crisis.

As in many Indian cities, this is chronic. The DJB says it supplies some 2.9 billion litres (650m gallons) of water a day, against demand of 4.2 billion litres. But that understates the gap. It estimates demand only from those with water connections, variously estimated at 60% and 80% of Delhi's 16m people. As for supply, some 15% is stolen and 40% lost to leakage. Many people queue at tankers, standpipes and boreholes fitted with handpipes.

With Delhi's population growing by 500,000 a year, "things are a little out of hand," admits Rakesh Mohan, the DJB's chief executive. As part of its effort to reverse this trend, the DJB plans a $246m project, $140m of it financed by the World Bank. The aim is to improve the DJB's management and the city's water infrastructure, and to move gradually to a continuous ("24/7") supply in two of 21 zones in Delhi, as a pilot scheme for the whole city.

The controversy was sparked by a local non-governmental group, Parivartan. Using right-to-information laws, it obtained documents on the award of a contract in 2001 to help design the project. These, it said, showed that the World Bank had bullied the DJB into appointing the Indian arm of PricewaterhouseCoopers, despite its having three times lost in the normal bidding process. The World Bank has defended its role in the evaluation of the bids as an excellent example of how it can "ensure transparency and fair competition".

The project itself is also under attack. It has raised the bogey of "privatisation", though in fact neither assets nor staff nor the right to set tariffs would be transferred. But in the two chosen zones, private firms would manage operations and maintenance, for a fixed fee. Four multinationals—Saur, Veolia and Suez of France, and America's Bechtel—are interested.

Last year the DJB's revenues covered only 60% of operating costs. Parivartan says that the plan would lead to an immediate hike for an average middle-class family from a monthly water bill of 192 rupees ($4.50) to 990 rupees. The World Bank says it has yet to agree a tariff policy with the DJB but that, although it believes tariffs should cover costs, its own projections are far below that. The DJB's Mr Mohan wants every family to get 6,000 litres a month free—enough for their basic needs—but to charge for all consumption above that.

He argues that buying private expertise in management is no different from buying pipes, pumps and meters. Sumita Dasgupta of the Centre for Science and Environment, a think-tank, sees "privatisation" as a side issue, as it is, in its fullest sense, inconceivable in India. The main question is where the water will come from. She also notes that the DJB's scheme depends on accurate and reliable water meters—which the DJB has so far been unable to deploy.

Delhi is also in the midst of a middle-class campaign against a rise in the price of electricity. The private companies that distribute electricity are under fire for their alleged poor performance. The DJB has an uphill struggle to persuade the public that its project is a good idea. That is perhaps why it has, say its critics, not even bothered to try, opening itself to suspicions that it is unleashing sharks into Delhi's water on the sly.

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Face value

The survivor

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Reuters

Why is Roman Abramovich still smiling?

THE contrast in fortunes can seem perplexing. Most of the theories about how Mikhail Khodorkovsky, ex-head of Yukos, an oil firm, offended Vladimir Putin, Russia's president, might be applied to Roman Abramovich, too. Or at least it seems that way.

Mr Khodorkovsky is said to have meddled in politics. Mr Abramovich is governor of the far eastern province of Chukotka. Yukos is accused of fiddling its taxes. Sibneft, Russia's fifth-biggest oil firm, which Mr Abramovich controls, has exploited tax “optimisation” schemes very efficiently. Like Mr Khodorkovsky, Mr Abramovich was among the first Russian bosses to exchange opaque business practices for better—and ultimately more profitable—corporate governance. But, according to some critics, Sibneft has not grown up entirely. In the courts of Moscow and the British Virgin Islands, Sibir Energy, another firm, is arguing that Sibneft illegally diluted Sibir's 50% stake in a west Siberian oil venture, a stake Sibir values at up to $2 billion, to less than 1% by underhand share issues: a favourite 1990s wheeze. (Sibneft hints that the dilution was part of a broader deal with a big Sibir shareholder.) With his yachts and multiple homes, Mr Abramovich has a more gratingly lavish lifestyle than did Mr Khodorkovsky. Yet while back-tax claims have wrecked Yukos, Sibneft seems to have settled a much smaller bill quietly and amicably. And while Mr Khodorkovsky, sentenced to nine years in jail for various alleged crimes, is now sharing a cell with ten other prisoners, Mr Abramovich, his successor as Russia's richest man, will this weekend watch his favourite toy, Chelsea Football Club, begin its defence of its English Premiership title.

One possible explanation is that in Russia “the rules” are different from those in the West. They are also liable to change suddenly. Indeed, understanding that has been perhaps Mr Abramovich's greatest talent. With Boris Berezovsky, one of the original “oligarchs”, he is said to have helped choreograph Mr Putin's succession to Boris Yeltsin. But Mr Abramovich understood Mr Putin better than his partner. From his exile in London, Mr Berezovsky recently threatened to sue Mr Abramovich over what he claims was the illegal acquisition of his assets after he was chased out of Russia. (A more charitable view is that Mr Abramovich simply spotted an opportunity.) Leonid Nevzlin, one of Mr Khodorkovsky's partners, alleges that Mr Abramovich—who pulled Sibneft out of a planned merger with Yukos after Mr Khodorkovsky's arrest—also orchestrated the Yukos affair. In court, Mr Khodorkovsky seemed to agree, lamenting the machinations of “mediocre business executives” who owned yachts and football clubs. But last week Mr Khodorkovsky backtracked, conceding that, while Mr Abramovich was “not the Apostle Peter,” he was not to blame for his downfall.

In contrast to these fallen tycoons, Mr Abramovich has been ingratiatingly generous to Mr Putin's government. He has pledged to finance a new national football stadium. In effect, he gave a stake in a TV company that he acquired from Mr Berezovsky to the Kremlin. That helped to prove that he was no political troublemaker. Despite his pharaonic lifestyle, in political terms Mr Abramovich's profile has always been low: as one experienced oligarch-watcher puts it, where others—however belatedly and self-interestedly—discovered political principles, Mr Abramovich “discovered compound interest”.

He does not influence parliament or cultivate foreign dignitaries as Mr Khodorkovsky did. Chukotka may owe more to business than politics. Mr Abramovich's defenders say that his interest in the desolate Arctic region is purely humanitarian. The grim lives of its 50,000-odd inhabitants have indeed improved since he took over. Sceptics dwell on the regional tax breaks Sibneft has enjoyed (though these, says the firm, have been more than compensated for by corporate and personal spending on social projects). Mr Abramovich visits his remote fiefdom less frequently then he once did, and seems ready to quit when his gubernatorial term expires in December. The Kremlin, however, may lean on him to stay on.

Never felt more like singing the Blues

Chukotka aside, he has been divesting himself of his Russian interests, including big stakes in Aeroflot and Rusal, an aluminium firm. Sudden changes in “the rules” are possible in the run-up to the presidential election due in 2008: social unrest or an economic downturn may push Mr Putin into populist, anti-oligarch measures. As Mr Berezovsky and Mr Khodorkovsky discovered, presidential successions (if there is a succession) can be risky. And however munificent his gifts, Mr Abramovich is outside the dominant Kremlin cliques of St Petersburgers and former KGB officers. He is a remnant from the Yeltsin era (when his nickname was “the purse”), and thus potentially vulnerable. His defenders say that he is not getting out of Russia but out of business, to spend more time with his football team.

A final ingratiating act may be to sell the 72% stake in Sibneft that he and his associates control. As the role of foreign firms in Russia's energy sector is now strictly limited, there is only one likely buyer: Gazprom, a state-controlled gas giant. (Rosneft, a state-owned oil firm, looks too debt-ridden after buying part of Yukos.) Last month Mr Putin said he knew of the Gazprom-Sibneft negotiations; his remarks were taken as definitive. In Russia's energy sector everything not forbidden now seems compulsory, as one old Soviet joke ran. The biggest obstacle may be public relations: how to finesse the handover of about $10 billion for an asset that Mr Abramovich, with Mr Berezovsky, got for peanuts a decade ago. But if the deal happens, the extravagant yet shy Mr Abramovich will bow out of Russia in a fittingly contradictory way: by helping the government to regain control of the country's energy resources, whose dubious privatisation made him and the other oligarchs billionaires.

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Italian banking scandal

Brothers in arms

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Ropi

Many reputations should suffer as a result of a scandal involving Banca Popolare Italiana and the Bank of Italy

"I JUST put my signature on it." These were the now notorious words of Antonio Fazio, governor of the Bank of Italy, on the phone to Gianpiero Fiorani, the chief executive of Banca Popolare Italiana (BPI), Italy's tenth-largest bank, shortly after midnight on July 12th. Mr Fazio had just given approval for BPI to buy a majority stake in Banca Antoniana Popolare Veneta (Antonveneta). "I'd kiss you right now, on the forehead," Mr Fiorani replied, in evident relief. (In an actual embrace, shown above, Mr Fazio is on the left.)

This news meant that BPI's bid for Antonveneta, in which a number of leading international banks have been involved, could proceed. It also seemed to spell certain defeat for ABN Amro, a big Dutch bank, with which BPI had been bitterly contesting control of Antonveneta since March. Antonveneta, based in Italy's wealthy Veneto region, is the country's ninth-largest bank but, by capitalisation, was around three times as large as BPI.

The conversation came to light because Mr Fiorani is under criminal investigation; magistrates had been intercepting his telephone calls for several weeks. His alleged offences include market-rigging connected to dealings in Antonveneta shares, false accounting and misleading the Bank of Italy (BOI), which oversees the banking system.

As supervisor, the BOI is responsible for ensuring the sound and prudent management of Italian banks. Each time a buyer of an equity stake in an Italian bank wishes to exceed certain thresholds—5%, 10%, 15%, 20%, 33% and 50%—it must seek permission from the BOI. Broadly speaking, a potential buyer must show that it has competent and honest management; a solvent balance sheet; and a sound plan for the target bank.

So the criminal investigations and the fact that two of the BOI's senior staff, worried about the strength of the bank's balance sheet, had refused to approve BPI's bid made Mr Fazio's decision hard to understand. That it was a grave error of judgment became obvious on July 25th when magistrates impounded BPI's shares (and those belonging to close allies) in Antonveneta. (The BOI declines to comment other than to say it has acted properly.) Two days later, Consob, Italy's stockmarket regulator, had no choice but to freeze BPI's offer for up to 90 days, as it also suspected that BPI's offer documents "seriously lacked important information". Then, on August 2nd, a judge ordered that Mr

Fiorani and BPI's finance director be suspended for the next two months.

But the story of BPI's attempt to buy Antonveneta not only raises serious questions about the BOI, Mr Fiorani and his allies. It also raises doubts about the judgment of banks that have lent their reputations and balance sheets to BPI, and about the ethics of some of them.

Based on *The Economist*'s examination of publicly available information, set out below, the first obvious question is: why did any leading bank want BPI as a customer? And the second: why was the BOI, with privileged access to information, so keen for BPI, rather than a bigger and healthier rival, to buy Antonveneta?

Why did any leading bank want BPI as a customer?

Through a buying spree, Mr Fiorani has transformed BPI, until recently called the Banca Popolare di Lodi, from a regional bank into one with a presence nationwide. For instance, it has 137 branches in Sicily after buying eight small banks there in just five years. Between 2000 and 2004, BPI spent roughly €6 billion ($7.4 billion at current rates) on acquisitions, often paying what one analyst describes as “very generous prices”.

These purchases have created a complex group: it comprises BPI, the quoted parent bank, which has about 60% of the group's retail branches, and two quoted subsidiaries, one of which is Bipielle Investimenti. Few analysts cover BPI (and even fewer its two quoted subsidiaries), and few big institutional investors own shares. Because of the group's constantly changing shape, comparative analysis of its results is tricky; it is difficult to measure how well acquisitions have performed.

Since 2000, the group has raised €3.6 billion from shareholders in six capital increases. BPI has used its branches to promote its shares (and other financial instruments) to customers, many of whom have become shareholders. Around 40,000 bought shares for the first time in its most recent issue for €1.5 billion in July, taking the total number to over 200,000.

Follow the money

But to the extent that these capital increases and other financial instruments have been paid for with money sitting in customers' accounts, BPI has not actually brought any new cash on to its balance sheet. Although it has improved BPI's capital ratios, such a switch of money from deposits to capital erodes future income by reducing lending possibilities.

An examination of the BPI group's accounts reveals aggressive accounting practices. BPI is treating some costs, such as those of capital increases and extraordinary personnel expenses, as intangible assets to be written off over several years rather than in one.

And how healthy is its balance sheet? The BOI assesses the solvency of a bank by the adequacy of its core capital—the minimum amount of capital a bank is required to hold to support its lending. Under EU rules, this must be kept above the minimum levels at all times. The starting point for the calculation is the net assets shown in a bank's accounts.

However, in BPI's case, there are doubts about the prudence of its accounts. Provisions against loans, which are lower than average, are one issue; if BPI's were adjusted to the level of, for example, Capitalia, a large Italian bank in which ABN Amro has a 9% stake, its net assets would fall by €337m. And BPI's 20% stake in Cassa di Risparmio di Bolzano, a savings bank, is overvalued by €209m when measured by the price that a purchaser, acquiring a majority interest, paid for a 10% stake last year. If the group's core capital at the end of 2004 were adjusted for just these two items, it would fall short of the mandatory level.

Moreover BPI has off-balance-sheet commitments which, if valued at market prices, would reduce its net assets further. It has promised to pay Deutsche Bank €330m in 2008 for 30m shares of Bipielle Investimenti that the German bank bought for only €198m in 2003. At the end of 2004, these were worth a mere €174m.

BPI will have to apply international accounting standards when it prepares its accounts for 2005. In the absence of reinforcement of its capital, application of these standards might expose the fragility of its balance sheet. For instance, off-balance-sheet commitments, such as that with Deutsche Bank, will have to be marked to market. And goodwill will be subject to an annual impairment test; if it is true that BPI has overpaid for its acquisitions, then substantial write-downs might be necessary.

In addition to its commitment to Deutsche Bank, BPI has others, mainly to the holders of minority stakes in subsidiaries. At the end of 2004, these amounted to €881m, over €500m payable in cash by mid-2005. To the extent that goodwill arises from the purchase in cash of these stakes, BPI's core capital would reduce further. This is because intangible assets do not count towards a bank's core capital.

But the BOI has postponed introducing a directive that would require banks to take account of these prospective commitments in the calculation of their core ratios. If these had been applied to BPI's core capital at the end of 2004 together with the other adjustments, then the bank would have fallen well short of mandatory levels.

Capital ratios are important to supervisors and depositors; investors are more interested in profits. But there is little consolation here. The 2004 accounts show that, at best, the parent company, BPI, the heart of the group with 577 branches, did little more than break even, if dividends from its subsidiaries are excluded. Even then, two factors favourably influenced its results. First, the marking-to-market of its portfolio of securities at the end of the year produced a net profit of €55m compared with a net loss of €9m the previous year.

Second, there was an increase of €30m in “expenses” recovered from customers' accounts, some (or all) of which may be explained by unusual entries in the final quarter. Astonished customers found charges, ranging from €30 to €125, for items such as “urgent commissions”, “post and telephone expenses” and “extraordinary commissions” on their bank statements dated December 31st, the bank's year end. Many asked for reimbursement, and some raised the matter with the judicial authorities. These charges imply a desperate attempt to boost profits.

There are also doubts about the quality of Bipielle Investimenti's profits. Its consumer-credit company booked a profit of €70m—representing an acceleration of future interest—from a securitisation of receivables. This flatters current profits and is only sustainable if consumer debt continues to increase, thereby allowing more securitisations. Another division enjoyed windfall profits of €26m because banker's drafts drawn on it had not been presented within the requisite time. Together, these items accounted for nearly half of Bipielle Investimenti's pre-tax profits.

Another serious concern is transparency. Nowhere is it apparent in the group's 2004 accounts that BPI has an equity investment of €154m in an obscure investment vehicle called Victoria & Eagle Strategic Fund (VESF), based in the Cayman Islands; this holds, or at least did in June, 4.1% of BPI. If BPI had bought the shares directly, disclosure in its accounts would have been mandatory. And, unlike an investment by BPI in its own shares, the investment in VESF is not deductible from BPI's core capital.

The pact of the matter

In spring 2004, Antonveneta was up for grabs; it was clear that a shareholders' pact, which owned 31% of the bank, would not be renewed in April 2005. The pact's members included ABN Amro, the Benetton family and several businessmen, one of whom was Emilio Gnutti, a controversial financier. These parties had formed the pact in March 2002 to provide stability of ownership and ensure autonomy for the bank's management.

One possibility was a merger between Antonveneta and Capitalia. This deal fell apart when the BOI would not allow ABN Amro—the biggest shareholder in both the banks—more than 15% of the merged bank, whereas ABN Amro wanted 20%.

Ropi

Mr Fiorani had a different idea; he began to promote BPI as a significant shareholder in Antonveneta. Mr Fazio, whose opposition to foreign ownership of Italian banks is well known, met Antonveneta shareholders. In early December, according to the Benetton group, he encouraged Gilberto Benetton, who was keen to sell his family's 5% stake, to be a good Italian when making his decision. Two weeks later, BPI extended the Benettons a loan of €325m to be repaid in cash or with its shares in Antonveneta.

Mr Gnutti controls Hopa, an investment company, of which Mr Fiorani is a director. And Hopa and BPI have reciprocal shareholdings. Mr Gnutti was keen to increase his stake in Antonveneta, and was a natural ally for Mr Fiorani. Their plan was to gain control of Antonveneta's board at

its annual general meeting at the end of April, an objective possible with around 30% of the votes.

Blind to his failings

Mr Gnutti has recently found himself in various scrapes. He has been found guilty of insider trading, though in Italy no conviction is definitive until confirmed by the final appeals court, which is yet to happen in Mr Gnutti's case. He is also currently on trial with a fellow director of Hopa, the chief executive of Unipol, an Italian insurer which has just launched a €5 billion bid for BNL, an Italian bank, for alleged insider trading in Unipol bonds.

Three reports by Consob show how Mr Fiorani and Mr Gnutti went about their business. BPI could not immediately buy a sizeable stake in Antonveneta. This was because it would need the BOI's permission; it had neither enough core capital nor a credible plan for the bank.

So between December 2004 and the end of February, BPI lent €552m at advantageous interest rates to 18 associates of Mr Gnutti, to buy 9.5% of Antonveneta. The Consob report states that there is a strong presumption that BPI promised these businessmen that it (or its allies) would eventually buy these shares and that they would make a gain. Another 20 people, including Stefano Ricucci, a property developer, bought a further 11.7% of Antonveneta, with BPI providing loans of €666m to 19 of them. BPI should have disclosed details of these loans to the BOI, but did not.

And press releases, which claimed to correct rumours about dealings in Antonveneta's shares, gave misleading information. For instance, on April 6th, BPI correctly stated its own stake but (falsely, on the basis of the Consob reports) denied there were any other agreements—written or oral—with third parties in respect of other shares. BPI's plan of deception was well under way.

When BPI told the BOI on February 11th of its intention to buy up to 14.9% of Antonveneta, the BOI could not have been more helpful. It approved the application over a weekend. The authorisation said that BPI should build up its stake only to the extent it took measures to strengthen its core capital. This was to ensure full and continuous respect for the minimum level. Normally, however, the BOI achieves this goal by insisting that a bank strengthen its core capital before giving permission. The BOI did not inform Antonveneta about the authorisation until April 23rd, an unusual delay; nor did BPI tell ABN Amro (which it met in March for talks) or the market.

But then ABN Amro made a move, announcing a cash offer for Antonveneta at €25 per share. If this offer succeeded, Mr Fiorani's plan would be in tatters. So to block ABN Amro, BPI would need a majority of Antonveneta's shares.

ABN Amro's offer could not proceed until the BOI gave its permission. However, when the Antonveneta pact expired on April 15th, the Dutch bank, the biggest shareholder with 12.7%, could increase its stake up to 33% if the BOI let it.

At the end of March, ABN Amro asked permission to acquire control, a process likely to take more than a month. To ensure it was free to buy shares as soon as possible after April 15th, it also asked—in the hope it would be granted without delay—to cross the 15% and 20% thresholds.

But, on April 19th, the BOI said ABN Amro could not increase its stake beyond 20%. The principal reason given was that the bank's request was tantamount to one for majority control and therefore needed the same scrutiny as the one to exceed the 50% threshold. This meant the Dutch bank could buy only another 7% of Antonveneta when the pact expired.

Meanwhile, again without informing Antonveneta, the BOI, applying a different standard, had authorised BPI to acquire up to 29.9%, taking only three days to approve BPI's request of April 4th.

The BOI was aware that BPI did not then have enough core capital to acquire more than 20%. However, it was receptive to the idea that BPI acquire voting rights for the remaining 10% by stock-borrowing. This involves renting shares for a limited period in return for a fee. The BOI thought BPI would buy these shares outright once it had strengthened its capital base.

But BPI was working to a different plan. After April 15th, when the Antonveneta shareholders' pact expired, large volumes of that bank's shares would be on the market. By April 18th at the latest, according to Consob's reports, BPI had formed a secret concert party, which included Mr Gnutti, Mr Ricucci and six others. Under stock-exchange rules, people acting in concert to acquire shares in a listed company are regarded as one. This is to prevent the circumvention of takeover law, such as that requiring a mandatory cash offer once a bidder exceeds a 30% threshold.

Altogether now

Between April 15th and 22nd, the concert party group, in some cases with further loans from BPI, conducted a huge buying operation from pre-arranged sellers and at pre-arranged prices. Except for those who became members of the concert party, all the people that BPI had financed earlier in the year sold their shares, making profits of €236m, including €110m by 15 associates of Mr Gnutti which an Italian court froze on August 2nd. The judge described these operations as “financial piracy”.

On April 27th, the BOI relented and gave ABN Amro permission to increase its stake to 29.9%. But by then, BPI's secret concert party had 46.7% of Antonveneta (including BPI's direct stake of 29.3%) and its allies at least a further 8.5%. By the time the BOI finally gave ABN Amro's bid the green light on May 6th, control of Antonveneta was already sewn up; any suggestion that the market would decide was farcical. Three days later, BPI announced a rival all-paper offer which, it claimed, was more valuable than the Dutch bank's cash offer.

But on May 10th, Consob ruled that BPI was part of an illegally undeclared concert party and said that the concert party must make an all-cash bid for Antonveneta. Suspicious that information was being withheld from the market, Consob had decided in mid-March to investigate all BPI's direct and indirect dealings in Antonveneta shares since November 2004.

Consob sent the detailed report behind its ruling to both BPI and the BOI, and even published it on its website. And soon after, as has been reported in the Italian press, members of the concert party (and most of those who had bought Antonveneta shares with BPI loans) were under criminal investigation for either alleged insider trading or market abuse.

Anything for a fee

Yet none of this put off a syndicate of ten banks, including BNP Paribas, Deutsche Bank, Dresdner Bank and the Royal Bank of Scotland, from making available on May 31st a facility of up to €4.9 billion to fund BPI's mandatory cash offer. Without this financing, BPI's bid would have been dead in the water. As security, these banks took a pledge on BPI's holding in Antonveneta, the very shares that magistrates subsequently impounded on July 25th. And despite all the unanswered questions, both Lazard and Dresdner Kleinwort Wasserstein (DKW), have been acting as financial advisers to BPI. Both Lazard and DKW decline to comment, as do banks involved in the syndicate.

Consob's report should have set alarm bells ringing, particularly at the BOI, not least because BPI and its concert party had acquired more than 30% of Antonveneta in flagrant violation of banking legislation. But the BOI did not begin an inspection at BPI until June 20th. Strangely, it started one at Antonveneta first.

Even before Consob's report, the BOI should have noticed a gaping hole in BPI's core capital. For technical accounting reasons, this hole opened up as soon as BPI's ownership of Antonveneta exceeded the 20% threshold. If BOI officials had monitored BPI's declarations to Consob, they would have noticed that BPI notified the market on April 19th that it had exceeded this threshold. According to calculations submitted by ABN Amro to an administrative court, BPI's core capital reached dangerously low levels after April 18th.

The hole was eventually plugged at the end of June by the last disposal in a series. Between May 18th and June 29th, BPI sold various minority interests of up to 20% in unquoted banking subsidiaries for €1.08 billion. The buyers were Deutsche Bank, Dresdner Bank and a company called Earchimede. (This company, in which BPI has a 12% stake, is controlled by companies associated with Mr Gnutti.) Deutsche Bank paid €721m; Dresdner Bank €220m and Earchimede €139m. In turn, Deutsche Bank sold to BNP Paribas half of each of the stakes it had just bought. BNP Paribas says that Deutsche Bank was its client.

Under banking rules, such disposals improve capital ratios only if they are genuine disposals. Temporary warehousing of stakes with third parties does not count.

Several aspects of the contracts, copies of which *The Economist* has seen, suggest these were not genuine disposals. For a start, BPI trumpeted these deals as industrial partnerships with the banks, but side agreements with Deutsche Bank give BPI the right to buy back within one year the shares that Deutsche Bank and Dresdner Bank had just bought, and for exactly the same amount these banks had paid. (For this right, Deutsche Bank charged fees of €75.6m.)

Then there is the price at which the deals were done. For instance, Deutsche Bank paid €183m for 10% of Cassa di Risparmio di Bolzano, when a stake of the same size sold for €79m just last year.

And BPI has given only a one-year guarantee on the level of dividends that these unquoted banks will pay; this hardly enhances the attractiveness of these illiquid stakes. Furthermore, the contracts contain none of the usual representations and warranties that purchasers usually require from sellers. The list of anomalies goes on.

An indication that these are temporary disposals would be if the purchasers had some right, even if indirect, to their money back from BPI. But BPI has stated in filings with Consob that no such arrangements exist. If this really is true, then Deutsche Bank appears to have acted with cavalier disregard towards its own shareholders' interests; it seems to have no exit route for its large investment. In fact, common sense suggests that Deutsche Bank has some undisclosed mechanisms—probably involving complex derivatives—to protect itself.

Deductive reasoning suggests that the disposals are in effect temporary; if so, the two German banks have helped BPI to window-dress its capital ratios. Deutsche Bank says: “We are comfortable with every aspect of this transaction, and will continue to co-operate with the authorities.”

In a call intercepted by investigating magistrates, Mr Fiorani, talking about an Earchimede board meeting on June 29th at which the contract with BPI was to be discussed, described the disposal to Earchimede as “temporary with a capital T”.

Whatever the case, BPI has not disclosed in stock-exchange filings important contracts with either Dresdner Bank or Deutsche Bank. No mention has been made of a significant stock-borrowing contract with Deutsche Bank relating to Antonveneta shares, or of derivatives contracts with Dresdner Bank for nearly 2% of Antonveneta shares.

The role of J.P. Morgan also raises questions. It acted as joint bookrunner for a share issue that ABN Amro undertook on March 30th to help finance its purchase of Antonveneta. At the same time, its Italian arm agreed to act as co-ordinating bank for ABN Amro in connection with its offer. However, BPI was then J.P. Morgan's counter-party in two derivatives contracts, dating from January 2005. One was a put-and-call agreement for 5m Antonveneta shares; the other a forward purchase of 5m Antonveneta shares. According to ABN Amro's advisers, J.P. Morgan did not disclose any conflict of interest to the Dutch bank before agreeing to act. J.P. Morgan says derivatives contracts are confidential as are its internal processes for managing conflicts. It claims ABN Amro was aware of the derivatives when it agreed (which it says was on April 12th) to act as co-ordinating bank.

Curtains

This six-month saga, which is gripping Italy, is now near its end. Criminal charges are almost certain. The interesting questions are: who will be charged and what will be the nature of the charges?

Mr Fiorani's tenure as chief executive of BPI is probably over, and his bank's takeover of Antonveneta is unlikely. New management at BPI would take a hard look at the bank's books. It would surprise few in Milan's financial circles if a new team at BPI were to find that the bank was, in reality, bust at the end of last year. (Ironically, as a result of its July share issue and other capital-raising deals, the bank is now flush with cash.)

If so, the question is whether Mr Fazio or others at the BOI knew or suspected this. If Mr Fazio did, this may explain why he wanted BPI to take over Antonveneta; merging a failing bank with a larger rival is one way of hiding the first's problems, if only temporarily. Or perhaps Mr Fazio's judgment was impaired by the closeness of his relationship with Mr Fiorani.

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Shareholder lawsuits

A blazing summer

Aug 11th 2005 | NEW YORK
From The Economist print edition

The sun has been shining on shareholders bringing class-action lawsuits against American companies

AMERICA'S new Class Action Fairness Act seeks to curb frivolous class-action lawsuits against companies in areas such as product liability and labour law, mainly by redirecting more of them to federal courts and so denying lawyers scope to “forum-shop” among biddable state courts. But before companies declare victory, they should reflect that the law of unintended consequences can sometimes be stronger than the law itself. The Private Securities Litigation Reform Act of 1995 was meant to curb frivolous class-action suits within the field of securities law. But in forcing class-action lawyers to raise their game, it has contributed to a new era of big lawsuits and even bigger settlements.

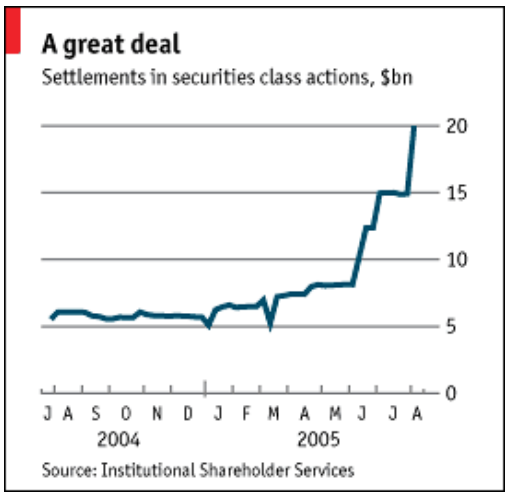
Total settlements swelled from $145m in 1997 (in 2004 dollars) to $5.5 billion last year, while the number of lawsuits stayed roughly constant, according to Cornerstone Research, an American litigation consultancy. This year will break all records. Institutional Shareholder Services, a research service which tracks class-action suits, says payments “in the pipeline”, agreed under pending and tentative settlements, have quadrupled from $5 billion in January this year to $20 billion in August (see chart).

That includes $7.1 billion so far in tentative settlements made by banks and other parties linked to Enron, including a $2.4 billion settlement by the Canadian Imperial Bank of Commerce announced on August 2nd; $6.1 billion in pending settlements by WorldCom and related parties; and a $2.5 billion pending settlement by Time Warner agreed on August 3rd.

Five banks have settled in the Enron suit, brought by the University of California as lead plaintiff. Seven have not. On August 3rd the University of California's law firm, Lerach Coughlin Stoia Geller Rudman & Robbins, sought to raise the pressure on Merrill Lynch, one of the banks that has not settled, by asking a judge in Texas to rule that Merrill had knowingly helped Enron to misstate earnings. Merrill responded by seeking to have the claim dismissed, saying that Lerach Coughlin failed to demonstrate that the investment bank caused losses to the law firm's clients.

For corporate America and its bankers, the fearsome size of recent class-action settlements may be tempered by the knowledge that these actions derive from the stockmarket bust of 2000-02. Once suits from this period are done, settlements may fall, said NERA Economic Consulting in a recent study. But for the law firms leading the class-action suits, and sharing in the settlements, these are the fat years for which they have worked adroitly since the securities-law reform in 1995.

That reform stopped lawyers from launching suits the moment they could find any small investor willing to lodge a first complaint. The role of “lead plaintiff” was reserved for the investor with most at stake, often an institution, who was expected to act responsibly.



Instead of putting the lawyers of the day out of business, the change forced them to think longer-term, and to cultivate the institutions they would need as clients. Trades-union and public pension funds, politically sympathetic to the principles of class action, were the readiest recruits. Private financial institutions were a harder sell, but the scandal-ridden stockmarket of 2000-02 made them angry too.

The law firms that have come out on top include Milberg Weiss, a New York partnership; Lerach Coughlin, founded last year by the west coast partners of Milberg Weiss; and the two firms that led the WorldCom litigation, Bernstein Litowitz Berger & Grossmann of New York, and Barrack, Rodos & Bacine of Philadelphia.

Class-action lawyers typically seek about one-third of the proceeds of a smaller settlement, but for large securities cases, this can shrink to 5-10% or so, according to filings on Institutional Shareholder Services' database. Still, given a $20 billion pipeline of pending and tentative settlements, a 10% cut means a bonanza of cash that the top law firms can plough back into making themselves even more formidable and indispensable. Lerach Coughlin's website boasts that the firm employs “dozens of former federal and state prosecutors and trial attorneys” supported by “an extensive group of in-house economic and damage analysts, investigators, and nine forensic accountants to aid in the prosecution of complex securities issues.”

There is little danger that other big, established law firms will try to break into the market, because that would mean upsetting their corporate customers. “It's very difficult to walk both sides of the street,” says Patrick Coughlin, a partner at Lerach Coughlin.

If a shadow does hang over this fine summer for class-action lawyers, it has been cast by court proceedings in Los Angeles, where an investor was charged in June with taking secret payments from a law firm in order to serve as plaintiff in more than 50 class-action lawsuits dating back years. The law firm, not named in the indictment, is Milberg Weiss, which says that it has been “unfairly implicated”, but is co-operating with a continuing federal investigation.

It is not hard to see some measure of “headline risk” at work. The fame of Milberg Weiss, and in particular of its former star litigator, William Lerach, now at Lerach Coughlin, may have made them more of a target. The affair is having no impact on the business of Lerach Coughlin, says Mr Coughlin, nor, he thinks, on that of Milberg Weiss. But there must be plenty of American companies hoping that it will.

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Oil

Frothy

Aug 11th 2005
From The Economist print edition

Speculators are betting on higher prices

ALMOST every week, it seems, brings another record oil price. On August 10th, the price of a barrel of West Texas Intermediate (WTI), the principal benchmark crude, breached $65 before closing a little below that mark. Traders already have $70 in their sights. You might think that this extraordinary bull run signals a severe shortage of crude oil. You would be wrong.

In fact, crude is plentiful. Members of the Organisation of Petroleum Exporting Countries (OPEC) are cranking out about as much oil as they can, thanks to the lure of high prices. Sheikh Ahmad Fahad Al Sabah, Kuwait's oil minister, said this week that OPEC's output is 30.4m barrels per day and rising: “These incremental volumes have led to global supply exceeding demand over the last two years.” At the end of July, crude stocks in the United States were at their highest since 1999.

So why are prices rising? Part of the reason lies in refining. One problem is a mismatch between the available grades of crude oil and refining technology. Because “sour” grades (such as those common in Saudi Arabia) are harder to refine into clean, low-sulphur fuels than “sweet” grades like America's WTI, refineries shun them; that pushes up the price of sweet benchmarks, such as WTI or Brent, which trade at hefty price premiums. American refineries have also been running flat out this summer to meet demand, and some half a dozen big plants have suffered breakdowns, causing tightness in downstream markets, for petrol and so forth. High downstream prices have in turn fed back into higher prices for crude.

Developments in the Middle East have also helped to push prices up. Iran's defiant stance on nuclear power has raised the spectre, however remote, of military action. King Abdullah, the new Saudi monarch, is not known as a price hawk. But observers worry that his accession has come at such a politically precarious time that he may favour higher prices, to give him cash to buy off dissent. This view was reinforced by news this week that America shut its diplomatic offices in the country briefly, because of threats of terrorist attack.

All this feeds what may be the biggest force moving the oil price: speculation. On one estimate, $22 billion of net new investment has entered the oil futures market this year, $8 billion of it flooding in since the end of June. As a result, forward prices have risen by even more than spot prices.

If inventories fall and forward prices remain unchanged, the spot price of oil could sprint ahead even without terrorist attacks in the Middle East, perhaps to $70, perhaps well beyond. This is the prevailing view in the market. But in a world awash with crude oil, just the opposite could be true too. If demand weakens sharply—say because the American or Chinese economies, the world's most eager guzzlers of oil, slowed unexpectedly—speculators could stampede out of the oil market and prices could fall quite markedly. The market's wild ride looks likely to continue for some time yet.

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The yuan

Chinese puzzles

Aug 11th 2005
From The Economist print edition

China's new currency basket is broader than most economists had expected

Get article background

ON AUGUST 10th, three weeks after China abandoned its decade-old peg to the dollar and moved to a managed float of the yuan against a basket of currencies, Zhou Xiaochuan, the governor of the People's Bank of China, revealed which currencies the basket contains. This came as a surprise. Singapore, which has operated a similar system since the 1980s, has never taken such a step. However, China's openness has limits: it is keeping to itself the weights attached to each currency.

Mr Zhou said that the dollar, the yen, the euro and the South Korean won have the biggest weights, but the basket also includes the currencies of Singapore, Britain, Malaysia, Russia, Australia, Thailand and Canada. The Hong Kong and Taiwanese dollars are conspicuously absent. Even so, the basket is much broader than expected. Most analysts had bet on only the dollar, the yen and the euro.

The choice of currencies (and hence presumably the weights), said Mr Zhou, depended not only on the pattern of China's trade but also on the sources of its foreign direct investment (FDI) and the currency composition of its debt. Stephen Jen, an economist at Morgan Stanley, has had a stab at estimating the weights. Using a weighted average of China's trade and FDI, he guesses that the dollar has a weight of 43%, the yen 18% and the euro 14%. This incorporates a higher dollar weight to reflect the importance of Hong Kong and Taiwan. The Hong Kong dollar is pegged to the greenback and all transactions between China and Taiwan are in dollars.

It is still unclear how the system will actually operate. In theory, if the dollar falls against the other currencies, the People's Bank of China should let the yuan rise against the dollar in order to hold the overall value of the basket steady. But this is at the discretion of the central bank. However, if this regime had been introduced in January, then as the dollar rose against the other currencies the yuan would have fallen against the dollar—which would hardly have pleased America's Congress.

China also announced this week a further liberalisation of foreign-exchange trading, allowing non-banks

to trade in the spot market and more banks to conduct forward trading. Currency swaps will also be introduced into the onshore market.

The reforms are aimed at making the domestic foreign-exchange market more liquid. That would allow banks and firms to hedge risks and so help them to handle uncertainty following the scrapping of the yuan's dollar peg. The central bank claims the measures will give the market a bigger role in setting the exchange rate. However, thanks to strict capital controls, the bank will retain its tight grip on the yuan.

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China's stockmarket

Hangover cure?

Aug 11th 2005 | HONG KONG
From The Economist print edition

A dispute over the planned release of government shares

Get article background

CHINA'S plan to remove the $250 billion overhang of state-owned shares that has depressed its stockmarket for the past seven years is proving harder than policymakers expected. In April, the country's securities regulator said it would resume the sale of these shares (also known as non-tradable or legal-person shares), which make up two-thirds of the domestic “A”-share market's total capitalisation, starting with a pilot programme of 46 companies.

Now, however, a row has blown up at the biggest and best-known of these firms—Baosteel, the mainland's leading steelmaker. Weijian Shan, managing director of Newbridge Capital, a Hong Kong venture-capital house, and one of Baosteel's four independent directors, says its particular scheme for non-tradable shares is both wrong and illegal. The steel group plans to compensate its current minority investors (some 22% of the total) for the fact that the state shares (the other 78%) will flood on to the market, further depressing the share price. Minority investors will get 2.2 extra shares for every ten they hold; and Baosteel promises to buy back shares and to pay an annual dividend of at least 0.32 yuan until 2007, which equates to a fat yield of 7.7% at the current share price.

This is affordable, because the group is minting money in a booming economy, but Mr Shan is opposed in principle to the unequal treatment of different shareholders. He estimates that minority investors will be paid at least three yuan per Chinese citizen by, in effect, the government. This may not sound like much, but there are nearly 1,400 listed Chinese companies facing a similar problem.

“There has to be a clear delineation of property rights,” says Mr Shan. “There is no reason to give away property rights especially when it will cost taxpayers, who are, in effect, the legal-person shareholders.” He also argues that announcing a guaranteed dividend amounts to share-price manipulation, breaking Chinese securities laws. Not surprisingly, he voted against Baosteel's scheme. The board, though, approved it, 10-1. A shareholder vote on August 12th is also expected to give it the nod.

This debate shows how tricky is the authorities' position. The Shanghai A-share market has fallen by 17% in the past year, largely because of the state-share overhang. This has stymied the development of proper capital markets and a real equity culture, which would help wean China off its dependence on bank lending. At some point, someone will have to pay to fix all this. It is likely to be the taxpayer.

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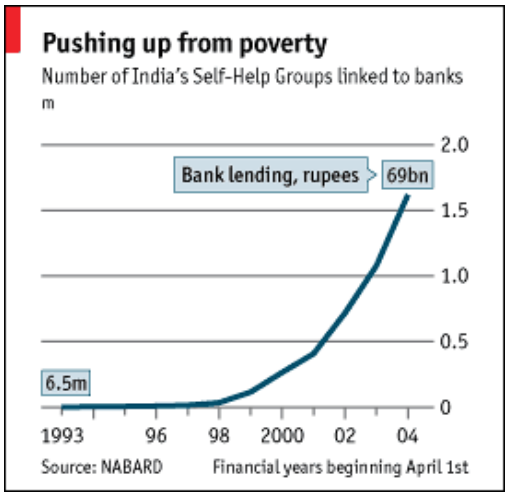
Microcredit in India

Helping themselves

Aug 11th 2005 | DELHI
From The Economist print edition

More loans for India's poor



Get article background

"IT IS the big moment. Couldn't be bigger," says Matthew Titus, of Sa-Dhan, an association of Indian microcredit lenders, of the outlook for his members. He is not alone in seeing microcredit—the lending of tiny amounts of money to people with even tinier assets—as at the point of take-off in his country. A new report from the central bank, the Reserve Bank, tackles some of the regulatory issues involved in expanding credit "at the bottom of the pyramid." It argues not just that microcredit helps the poor, but that it allows banks to "increase their business, enhance their profit and spread the risk."

Microcredit is already a flourishing business, reaching 8m-10m households, Sa-Dhan believes, mainly through "Self-Help Groups" (SHGs). These, supported by banks, notably the government's National Bank for Agriculture and Rural Development (NABARD), typically bring together about 15 women, who pool savings for a few months, allocate them to members who need small amounts temporarily, and are then eligible for a bank loan. The number of SHGs is expanding quickly (see chart). A package of measures announced in this year's central-government budget is expected to provide a further fillip to the microcredit industry.

A billion-rupee boost

In his budget speech in February, the finance minister, Palaniappan Chidambaram, promised to promote microfinance institutions (MFIs)—mostly charities—"in a big way", and to help them to act as intermediaries between banks and borrowers. He doubled, to 2 billion rupees ($46m), a fund devoted to providing the MFIs with capital—to help, for example, organise SHGs. He promised new legislation that would give them an official status and a clear regulatory framework. He also allowed them for the first time to borrow money from abroad.

Despite its recent growth, however, microcredit is far less widespread in India than in neighbouring Bangladesh. A World Bank report published last December reckoned that it amounted to no more than "a drop in the ocean", touching fewer than 5% of India's poor. In Bangladesh, by contrast, it is estimated to reach some two-thirds of potential borrowers.

One reason India has lagged, oddly, is the determination of its post-independence rulers to free poor farmers from the clutches of local moneylenders. The upshot is, in Mr Titus's envious words, “a banking infrastructure to die for”—66,500 branches (mostly of public-sector banks), 98,000 agricultural credit co-operatives and a post office with 154,000 outlets. Yet most of India's rural poor still do not have access to formal finance, the World Bank study found. Moneylenders are no longer as dominant as they were, but they still play an important role, especially among the very poor. When poor people do manage to borrow from banks, they often have to pay bribes that make the total cost of finance no less usurious.

So there is a huge gap. But expanding to fill it is expensive. Microcredit is a time-consuming business, where it is hard to achieve a big increase in market size without a commensurate increase in costs. Some see the solution in technology. Vishnu Dusad, boss of Nucleus Software, one of India's leading suppliers of retail-banking systems, says he hopes to bring down the cost of lending so that loans of 100 rupees will be feasible.

Nucleus is working with an MFI start-up, Ujjivan, whose initial intended market will be the poor of Bangalore, India's information-technology hub. Ujjivan's Samit Ghosh aims to cut operating costs from the MFIs' typical 95% of income to 70% or less.

Many agree that adapting commercial-banking systems to MFIs might allow them to cater for more customers, raise efficiency and cut back-office costs. But the real challenges are at the front end, in the villages themselves. Ajay Tankha, a Delhi-based microfinance consultant, says that there is already evidence that some SHGs are overstretched. Microcredit, he says, can ruin as well as rescue the poor, if not enough is done to help and advise the borrower. And in that area, computer programmes remain a poor second-best.

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Commerzbank

The bank that shrank

Aug 11th 2005 | FRANKFURT
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Less ambitious, healthier—and more attractive to potential buyers

TOPPED by a 41-metre red and white mast, the Commerzbank tower in Frankfurt is Europe's tallest office building. The bank's trading floor, across town, is also one of Europe's largest. Although these relics of the bank's recent delusions of grandeur remain, Klaus-Peter Müller, the bank's Napoleon-sized chief executive, has been reducing his empire.

The new size and financial health of Germany's fourth-largest bank have attracted fresh takeover rumours. The latest suitors are said to be BNP Paribas of France and Santander Central Hispano of Spain. Such speculation drove the share price up by 19% in the week after August 3rd, when the bank reported more stable earnings.

The watershed for Mr Müller was the departure last September of Mehmet Dalman, head of investment banking, who had tried to make the bank a global player in equities, head-to-head with Goldman Sachs, Morgan Stanley and Deutsche Bank, his former employer. That meant big operations and complex trading books in London, New York and Tokyo, with an army of highly paid staff. It also meant putting a big chunk of the firm's equity at risk daily.

Starting in November, the corporate and investment bank was restructured under Nicholas Teller, a German-educated Briton. The Tokyo office was closed and New York's strength was cut by three-quarters. Some trading operations in London survive. In all, 500 investment bankers went. The investment bank had lost €600m ($720m) on securities positions in the previous three years, but its demands on capital have shrunk by 30% and its risk exposure by 50%.

Commerzbank is now concentrating on its German retail and corporate customers (it has 5% and perhaps 15% of the respective markets). For German companies at home and abroad it continues to provide hedges and other derivatives. But it is no longer making big, risky bets. For retail customers Commerzbank is still big in equity derivatives, warrants and other speculative paper, which it lists on the Stuttgart stock exchange. It is rebuilding its presence in foreign exchange. So it has not vanished from the market, but it can no longer be called a *Grossbank*—a big universal bank to rival Deutsche Bank, Germany's biggest bank, or even Dresdner Bank, the number three, owned by Allianz, an insurer. In fact Mr Müller is more inclined to compare his bank with Sal Oppenheim and Metzler, two small but highly profitable corporate-finance and investment houses in Frankfurt.

This is a big change for a bank whose costs were out of control a year ago. Commerzbank has even been able to do some shopping. It bought the insolvent Schmidt-Bank, adding 350,000 customers in Bavaria; and it took full control of BRE Bank in Warsaw and launched mBank, an online bank, there. It also tried to buy BHF-Bank, once rated as Germany's best merchant bank, but was outbid by Oppenheim. It is a contender for BHW, a financial-services company with 4m customers. And it is looking for bargains in Russia, Ukraine and Turkey, where profits can grow faster than at home.

Mr Müller says that profitability is more important than market share. He estimates that his long-term cost of capital is 10.25%. The bank beat that in the first half, with an annualised return on equity after tax of 12.6%, but the chief executive's expectation for the whole year is only 8%.

Will anyone buy Mr Müller's shrinking bank? He himself is happy to carry on or sell, as long as the deal is good for shareholders, customers and employees. Commerzbank is a perennial subject of takeover rumours, and the talk has intensified since the purchase in June of HVB, Germany's second-biggest bank, by UniCredit of Italy. A buyer would get a reasonable share of the German corporate market and a foothold in central Europe. British or Spanish banks might balk at the low profitability and poor retail base; a Dutch or French bank may not be so sniffy. Any purchaser would have to deal with Germany's unions and rigid labour laws if it wanted to cut more of the 25,000 remaining employees in the country.

Firing someone costs about a year's salary.

That may be more of a deterrent than some negative recent publicity. Three former employees and one still at the bank are being investigated in connection with a Russian privatisation scam, but no charges have been made. There was also a fuss in the press about the promise of guaranteed bonuses to keep labour representatives happy.

A buyer would also acquire a landmark that dominates the Frankfurt skyline. At night, parts of the tower glow Commerzbank yellow. A change of corporate colour should only involve changing a few light bulbs. There should be enough staff left to do the job.

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Economics focus

A working model

Aug 11th 2005
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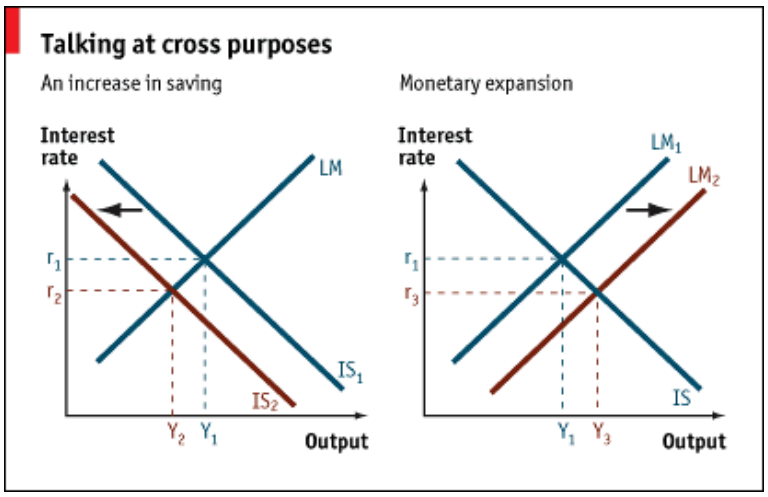

Is the world experiencing excess saving or excess liquidity?

WHEN *The Economist*'s economics editor studied macroeconomics in the 1970s, the basic model for understanding swings in demand was the so-called IS-LM framework, invented by Sir John Hicks in 1937 as an interpretation of Keynes's "General Theory". In recent years it has gone out of fashion, dismissed as too simplistic. That is a pity, for not only does the model seem more relevant than ever today, but it also casts useful light on why bond yields are so low.

America's Federal Reserve raised short-term interest rates again this week, to 3.5%, its tenth increase since June 2004. Yet over that period, long-term bond yields have fallen to historically low levels. Indeed, virtually everywhere around the globe real bond yields are unusually low. The most popular explanation is that there is a global glut of savings, which has driven yields down. However, while some parts of the world, notably Asia, may save more than they need to, it is not obvious that the world as a whole is doing so. Over the past couple of years, global saving has risen as a share of GDP, but so too has investment. By definition, global saving must equal global investment; what really matter are *ex ante*, desired rates of saving and investment which may have caused bond yields to decline. An alternative explanation, preferred by some economists, is that bond prices, like other asset prices, have simply been pushed up by excess liquidity (ie, yields have been pushed down).

The IS-LM model helps us to understand these two opposing theories. Originally devised for a single closed economy, it can today be more realistically applied to the global economy. Its main virtue is that it brings together both the real and the financial parts of the economy. The IS (investment/saving) curve represents equilibrium in product markets, showing combinations of output and interest rates at which investment equals saving and hence the demand for goods and services equals supply. The IS curve slopes downwards, because a higher interest rate reduces spending and so lowers the level of output at which demand equals supply.

The LM (liquidity/money) curve represents equilibrium in the money market, showing combinations of output and interest rates where the demand for holding money, rather than interest-bearing assets, such as bonds, equals the supply of money. This curve slopes upwards, because a rise in income increases the demand for money and so raises the interest rate at which the supply of and demand for money are equal to one another. (A rise in rates reduces the demand for money because it raises the opportunity cost of holding non-interest-bearing assets.)

The point at which the two curves intersect is the only combination of output and interest rates (ie, bond

yields) where both the goods and financial markets are in balance. Too much economic commentary seems to assume that the IS curve alone (ie, the balance between saving and investment) determines bond yields. But yields also depend on the LM curve, which represents, in effect, the choice between holding money or bonds.

Reading between the lines

The left-hand chart shows the economy in equilibrium at interest rate r1 and output Y1. If desired saving increases relative to investment (ie, there is excess saving), the IS curve shifts to the left to IS2. Interest rates fall (to r2), and so also will output (to Y2). This does not fit the current facts: last year the world economy grew at its fastest pace for almost three decades, and this year remains well above its long-term average growth rate.

The right-hand chart illustrates the alternative theory. A loose global monetary policy shifts the LM curve to the right, to LM2. Bond yields again fall, to r3, but this time output increases. In contrast to a shift in the IS curve, the economy has instead moved along the IS curve: lower interest rates stimulate global output and hence investment. This seems to fit the facts much more comfortably.

Bond yields are low largely because central banks have created too much liquidity. Despite rising short-term interest rates in America, monetary policy is still unusually expansionary. Average short-term rates in America, Europe and Japan have remained below nominal GDP growth for the longest period since the 1970s. In addition, America's loose policy has been amplified by the build-up in foreign-exchange reserves and domestic liquidity in countries that have tied their currencies to the dollar, notably China and the rest of Asia. As a result, over the past couple of years, global liquidity has expanded at its fastest pace for three decades. If you flood the world with money, it has to go somewhere, and some of it has gone into bonds, resulting in lower yields. Or, more strictly, bond prices have been bid up until yields are so low that people are happy to hold the increased supply of money. In its latest annual report, the Bank for International Settlements suggests that the fact that the prices of all non-monetary assets (including bonds) have risen could indeed reflect an effort by investors to get rid of excess liquidity.

In fact, the two theories are not mutually exclusive. Too much saving relative to investment may well have gone hand in hand with excess liquidity, ie, both the IS and LM curves have shifted downwards. Central banks' monetary easing was, after all, partly in response to a fall in investment after share prices slumped. However, the current rapid pace of global growth suggests that excess liquidity is the prime cause of low bond yields. The snag is that central banks will eventually have to mop up the overhang of liquidity and bond yields will then rise.

Why isn't excess liquidity generating inflation? The basic IS-LM model assumed that the price level was fixed, and thus its inability to explain high inflation rates in the 1970s and 1980s hastened its fall from grace. If an economy is at full employment, an increase in money leads to higher prices, not lower bond yields. Today, however, the model may be more relevant because the entry into the world economy of cheap labour in China and other emerging economies is helping to hold down inflation. In a world of low inflation, IS-LM rides again.

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Climate change

Heat and light

Aug 11th 2005
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An unexplained anomaly in the climate seems to have been the result of bad data

Get article background

CLIMATOLOGY is an inexact science at the best of times. Unfortunately it has become, over the past couple of decades, a politically charged one as well. As the debate about global warming—and what, if anything, to do about it—has gathered pace, uncertainties in the data that would be of merely academic interest in other disciplines have acquired enormous practical significance. And one of the most curious uncertainties of all is the apparent discrepancy between what is happening to temperatures at the Earth's surface and what is happening in the troposphere—the lowest layer of the atmosphere, and thus the part that is in contact with that surface.

The troposphere is where most of the air is found and where most of the weather occurs. Computer models predict that, if global warming is really happening, temperatures in the troposphere should rise along with those on the surface. Recorded surface temperatures are, indeed, rising. However, both data from weather balloons and observations made by satellites suggest that temperatures in the troposphere have remained constant since the 1970s. Over the tropics they may even have dropped. This counter-intuitive result has caused sceptics to question how much warming, if any, is actually going on.

There are, of course, three possibilities. One is that the sceptics are right. A second is that the models are wrong. And the third is that there is something wrong with the data. Three papers published in this week's issue of *Science* suggest that the third possibility is the correct one.

Day and night

The first of these studies, conducted by Steven Sherwood of Yale University and his colleagues, examined data from weather balloons. For the past 40 years, weather stations around the world have released these balloons twice a day at the same time—midday and midnight Greenwich Mean Time. Each balloon carries a small, expendable measuring device called a radiosonde that sends back information on atmospheric pressure, humidity and, most importantly for this study, temperature.

Unfortunately, data from radiosondes come with built-in inaccuracies. For example, their thermometers, which are supposed to be measuring the temperature of the air itself (that is, the temperature in the shade) are often exposed to, and thus heated by, the sun's rays. To compensate for this, a correction factor is routinely applied to the raw data. The question is, is that correction factor correct?

Dr Sherwood argues that it is not. In particular, changes in radiosonde design intended to reduce the original problem of over-heating have not always been accommodated by reductions in the correction factors for more recently collected data. Those data have thus been over-corrected, reducing the apparent temperature below the actual temperature.

Dr Sherwood and his colleagues hit on a ruse to test this idea. Because weather stations around the world release their balloons simultaneously, some of the measurements are taken in daylight and some in darkness. By comparing the raw data, the team was able to identify a trend: recorded night-time temperatures in the troposphere (night being the ultimate form of shade) have indeed risen. It is only daytime temperatures that seem to have dropped. Previous work, which has concentrated on average values, failed to highlight this distinction, which seems to have been caused by over-correction of the daytime figures. When the team corrected the erroneous corrections, the result agreed with the models of the troposphere and with records of the surface temperature. The improvement was particularly noticeable in the tropics, an area that had previously appeared to have high surface temperatures but far cooler tropospheric temperatures than had been expected.

The second piece of work looked at satellite measurements of tropospheric temperatures. For the past two decades, microwave detectors, placed on a series of satellites flying in orbits that take them over both poles, have been used to calculate the troposphere's temperature. (Microwaves radiated from the atmosphere contain a host of information about its temperature and humidity.) Here, too, the data are problematic. Because the satellites are looking down through the whole atmosphere, measuring the temperature of the troposphere requires subtracting the effects of the stratosphere—the atmospheric layer above it. But when this has been done, the result suggests, like the over-corrected data from the radiosondes, that the troposphere is cooling down relative to the surface.

However, Carl Mears and Frank Wentz of Remote Sensing Systems, a firm based in Santa Rosa, California, think that this trend, too, is an artefact. It is caused, they believe, because the orbital period of a satellite changes slowly over that satellite's lifetime, as its orbit decays due to friction with the outer reaches of the atmosphere. If due allowance is not made for such changes, spurious long-term trends can appear in the data. Dr Mears and Dr Wentz plugged this observation into a model, and the model suggested that the apparent cooling the satellites had observed is indeed such a spurious trend. Correct for orbital decay and you see not cooling, but warming.

The third paper, by Ben Santer of the Lawrence Livermore National Laboratory in California and his colleagues, argues that it is, indeed, errors in the data that are to blame for disagreements between the predictions of computer models about how the troposphere should behave and what the weather balloons and satellites actually detect. Dr Santer's team compared 19 different computer models. All agreed that the troposphere should be getting warmer. Individual models have their individual faults, of course. But unless all contain some huge, false underlying assumption that is invisible to the world's climatologists, the fact that all of them trend in the same direction reinforces the idea that it is the data which are spurious rather than the models' predictions.

It is, nevertheless, doubtful that these papers will end the matter. Studying the climate is a hard problem for three reasons. The system itself is incredibly complex. There is only one such system, so comparative studies are impossible. And controlled experiments are equally impossible. So there will always be uncertainty and therefore room for dissent. How policymakers treat that dissent is a political question, not a scientific one.

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Solar power

Solid sunshine

Aug 11th 2005
From The Economist print edition

A new way of storing the sun's rays in a useful form

MIX a pile of manure with some zinc oxide, angle a few giant mirrors towards the mixture, turn on the sun and steam the result. It may not sound appetising, but Michael Epstein and his colleagues at the Weizmann Institute of Science, in Israel, think that this recipe represents a novel way of collecting solar energy to generate what many hope will be the fuel of the future—hydrogen.

Readers who remember their chemistry lessons may recall mixing zinc with hydrochloric acid in a test tube and standing by, lighted splint in hand, ready to ignite the hydrogen that is given off. (Metallic zinc reacts with the chlorine in the acid, leaving hydrogen behind.) Zinc reacts similarly with water—or, rather, steam—in this case stripping the oxygen from H_2O and, once again, leaving the hydrogen. Industrialising that process, though, relies on finding a cheap way of turning the zinc oxide that results back into metallic zinc, so that the material can be recycled. And this, courtesy of the Weizmann Institute's Solar Tower laboratory, is what Dr Epstein has done.

Corbis

The tower's 64 seven-metre-wide mirrors track the sun and focus its rays into a beam with a power of up to 300 kilowatts (see picture). In Dr Epstein's experiment, which he outlined at the recent International Solar Energy Society conference in Orlando, Florida, the beam was used to heat a mixture of zinc oxide and charcoal. The charcoal (which is pure carbon) reacted with the oxygen in the zinc oxide, releasing the zinc. This instantly vaporised and was then extracted and condensed into powder.

At the moment, the cheapest way of making hydrogen is a process called reformation, which also uses steam, but reacts it with natural gas, a fossil fuel. Dr Epstein thinks that if his process were scaled up, it would cost about the same as reformation. It would also have the advantage over reformation that no fossil fuel need be involved (the charcoal can be made from agricultural waste, such as manure), and so there is no net contribution of climate-changing carbon dioxide to the atmosphere. And the other way of using solar power to make hydrogen—generating electricity using solar cells and then using that electricity to split water into its component gases—is vastly less efficient than Dr Epstein's method.

In the meantime, the powdered zinc produced can be employed in a different form of energy technology—zinc-air batteries. These are used to power certain sorts of electronic device. So, even if your car never runs on second-hand solar energy, one day your laptop might.

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Private spaceflight

Sinatra, eat your heart out

Aug 11th 2005
From The Economist print edition

Got $100m? Then an American firm can fly you to the moon

SIGHS of relief all round greeted the touchdown of STS 114, as the latest space-shuttle flight is known to the cognoscenti. In truth, this was the most mollycoddled mission in NASA's history, so if anything serious had gone wrong with it the agency would probably not have emerged intact from the wreckage. Now, although there are still doubts about whether there will ever be an STS 115, the show can go on. And the next act, expected within a few days—or weeks at most—will be the unveiling of detailed plans for a return to the moon.

But NASA has been upstaged. This week, Space Adventures, a firm based in Arlington, Virginia, announced that it is offering a private trip to the moon for two fare-paying passengers. The catch is the fare—the small matter of $100m a seat.

Although it may seem implausible that a tiny company could offer such a trip, Space Adventures has already organised travel to the International Space Station for two fare-paying passengers, and a third is due to fly in October, so its proposals for lunar tourism need to be taken seriously. And the firm is not actually offering a holiday *on* the moon. That would be impossible with existing spacecraft. Instead, tourists will follow a figure-of-eight path that will take them swooping low over the surface of the far side of the moon, and then back to Earth.

Space Adventures would not, of course, transport the lunar tourists in its own fleet. The hardware and the pilots would, like those for its trips to the space station, be provided respectively by RSC Energia, Russia's leading spacecraft-maker, and by the Russian Space Agency. However, unlike the space-station jaunts, a trip around the moon would not be a mere commercial recapitulation of a type of mission that had already been flown.

Soyuz, Russia's manned spacecraft, is a tried and tested design, but it has never been to the moon. For that to happen, a *Soyuz* capsule will have to be launched into orbit on one booster rocket, and then dock with a second booster that has been launched from Earth as a separate payload by yet a third booster. The second booster will provide the oomph necessary to get to the moon and back. Alternatively, for the full extraterrestrial experience, the *Soyuz* might dock with the space station, allowing passengers a few days in Earth orbit before they go on to the moon.

Eric Anderson, the president of Space Adventures, says that one of the things that makes *Soyuz* suitable for this mission is that during the cold war space race, the Russians were developing a stripped-down version of *Soyuz* for a trip to the moon. Nevertheless, some extra research and development would be necessary, as well as modifications to the navigation system, and the enlargement of the craft's window. The latter will have the double benefit of giving passengers a better view and allowing high-resolution pictures of the surface of the moon to be taken. Surprisingly, such holiday snaps would be the first close-up, high-res photos of the lunar surface, which would add a gloss of scientific respectability to the whole enterprise.

According to Mr Anderson, the $200m mission fee will cover the cost of a test launch with an unmanned *Soyuz*, as well as the costs of the modifications. And if somebody stumped up money now, the mission would be ready to fly in five years. The big question is: who would pay $100m? Space Adventures' market research suggests that at least 1,000 people could afford to do so. Whether any of these billionaires are also brave enough to venture into deep space, and to the far side of the moon, remains to be seen.

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Materials science

Pasta alla fisica

Aug 11th 2005
From The Economist print edition

Physicists have solved the long-standing puzzle of how spaghetti breaks

IT WAS a problem that baffled the master himself. Richard Feynman—maverick physics genius, Nobel laureate and father of modern quantum theory—could not work out why, when a strand of dried spaghetti is snapped, it almost never breaks in half but instead fragments into three or more pieces. At dinner with Daniel Hillis, an old friend and computer scientist, the two became obsessed with this and spent hours theorising and experimenting. In the end, they left with a kitchen full of pulverised pasta and no reasonable answer.

Basile Audoly and Sébastien Neukirch of the University of Paris VI think, however, that they have succeeded where Feynman failed. Their calculations, revealed in a forthcoming paper in *Physical Review Letters*, suggest that the key to the problem lies in so-called flexural waves. Each time part of a bent strand breaks, a series of these waves ripples down the length of the pasta. The mistake Feynman probably made was to assume that the strain released when a bent strand breaks allows the two half-strands to relax and become straight again. Instead, according to their equations, the passing waves cause parts of the daughter strands to curve even further. This triggers other breakages which, in turn, trigger further waves, causing the strand to fragment.

To put their mathematical solution to the test, they devised a rigorous experiment. And, like all good researchers, they describe their materials and methods in a way that allows others to repeat what they did: “A Barilla no. 1 dry spaghetti pasta of length L=24.1cm was clamped and bent into an arc of circle,” they write. “Twenty-five experiments were carried out with various pasta diameters.” By snapping 1,000 photos per second as they released the bent strands, they were able to see the travelling waves and to show that the motion of the strands followed their equation exquisitely. Videos of all this can be viewed here.

Dr Audoly's and Dr Neukirch's research does have a serious point, of course. The steel struts that help to hold up skyscrapers and bridges are slightly less trivial examples of thin rods whose tendency to break needs to be understood. Knowing the mechanisms by which these rods fragment is important not only for designing such structures but also for reconstructing what has gone wrong when one fails.

Having out-thought Feynman, though, it is hard to see what should be next on the pasta research agenda. Perhaps a suitably profound problem is that of the slowing down of time—a well-established part of the theory of relativity. Or, to put it in pasta terms, does a watched pot take longer to boil?

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Correction: trees and carbon

Aug 11th 2005
From The Economist print edition

In "Down with trees" (July 30th) we said that a team of American and Brazilian scientists found that trees in the Amazon were returning their carbon to the atmosphere after five years. The researchers have asked us to make it clear that this is the age of the carbon they found in the local rivers. That carbon is derived from leaves and twigs. The bulk of the carbon taken into a tree remains in its trunks and roots until it dies and decomposes. The average turnover time for this carbon is more than a century. Sorry for the confusion.

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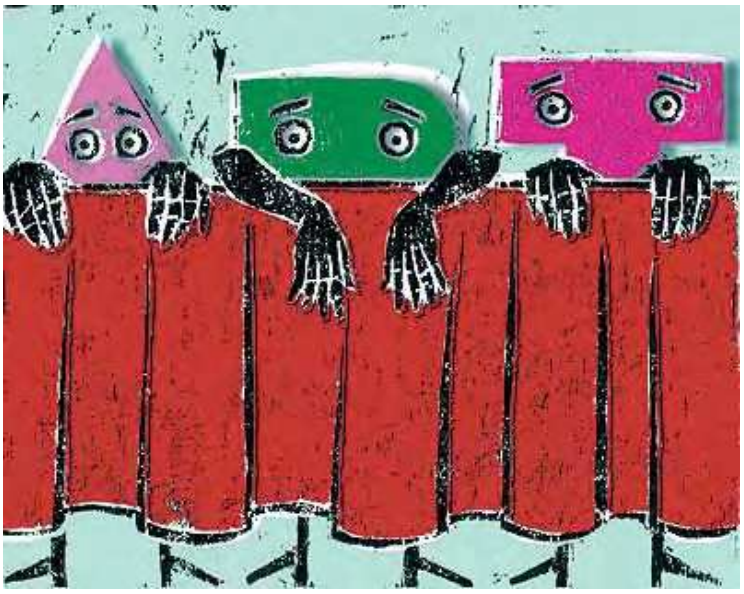
The meaning of art

Art smarts

Aug 11th 2005
From The Economist print edition



Though art retains its mystery, a couple of books throw light on this and that

WHAT is art for and what good does it do? Two centuries ago, Kant and Hegel spent much of their lives contemplating questions about art and aesthetics. Many others have done so since. The latest are two studies, from either side of the Atlantic, by Michael Kimmelman and John Carey. The authors are professionally involved in the arts, Mr Kimmelman as chief art critic at the *New York Times* and Mr Carey as a professor of English literature at Oxford University. Scholars both, they are prodigious readers, listeners to, and students of, art. Yet both their books are at their most impressive when the authors seem to be trying the least.

Mr Kimmelman, a gifted piano student as a boy, returned more seriously to the keyboard in 1999 when he entered, and went on to the final round, of an amateur piano competition in Fort Worth, Texas. Organised by the Van Cliburn Foundation, which since 1962 has presented the world's leading piano competition for young professionals, the competition brought 90 people, who neither taught nor performed professionally, to Texas.

Mr Kimmelman's article about his fellow pianists—a numismatist, two flight attendants, a hairstylist and a former crack addict who had been jailed for burglary and who found taking up music helped him recover—raised a sizeable correspondence from people who are not artists by profession, but for whom art adds an important other dimension to their lives. It was this idea, so emblematic of the author's own life, that spawned the book.

“I have come to feel”, he writes, “that everything, even the most ordinary daily affair, is enriched by the lessons that can be gleaned from art. Put differently, this book is, in part, about how creating, collecting, and even just appreciating art can make living a daily masterpiece.”

The Accidental Masterpiece: On the Art of Life and Vice Versa
By Michael Kimmelman

Penguin; 224 pages; $24.95

Buy it at
Amazon.com
Amazon.co.uk

What Good Are the Arts?
By John Carey

The portraits Mr Kimmelman presents in order to illustrate his point are loosely associated. There is the artist who created without lifting a finger: Ray Johnson, a coolly analytical man who was fascinated by numbers and who killed himself a decade ago at the age of 67 on January 13th (6+7=13, his friends noted), having first telephoned an old colleague, William Wilson, whose name contains 13 letters. There is the accidental artist: a German policeman photographed for posterity in 1927 hanging on to the bottom of a zeppelin that had broken its moorings. And there is the illuminating artist, a Baltimore dentist who, in the course of a lifetime, collected 75,000 lightbulbs and created the Museum of Incandescent Lighting.

Faber and Faber; 304 pages; £12.99. To be published in America by Oxford University Press in December; $25

Buy it at Amazon.co.uk

But his best example is Pierre Bonnard, whose accidental encounter with a young, elfin woman alighting from a Paris tram in 1893 led to an intense relationship that would last until her death half a century later. Easily derided after his death as a facile, if accomplished, colourist, it is Bonnard's secretive, moody portraits of the woman, Marthe, many of them posed in the privacy of her bathroom, that mark him out as a painter of elegy. Often described as a painter of pleasure, one critic observed, he was something even more rare: a painter of the effervescence of pleasure and the disappearance of pleasure.

Mr Kimmelman's book works best when he describes the ineffable by showing rather than telling. His brief anecdote about how Bonnard once asked a model not to sit still, but to move around the room, is far more effective than a convoluted explanation about the difficulty of painting presence and absence at once.

Too much telling, by contrast, is Mr Carey's error. What is a work of art, is high art superior, do the arts make us better, can art be a religion? One after the other, Mr Carey head-butts these questions. The result, however, is that he ties himself up in knots. Unable to reach any conclusion about what art is, he turns instead to what it is not. There are plenty of things that are not works of art: for example, human excrement. Probably. But what about Piero Manzoni, an Italian artist who died in 1963 after creating an “edition” of 90 tin cans each containing 30 grams of his own excrement? The Museum of Modern Art, the Tate Gallery and the Pompidou Centre snapped them up. More fool them, you say. Others would agree, but they would be no closer to defining what art is.

Far, far better is the second half of the book in which Mr Carey seeks to persuade us that the greatest of all art forms is not painting or music but literature, and English literature specifically. Uninflected and without gendered nouns, English was uniquely placed to offer Shakespeare the linguistic pliancy and suppleness he needed to turn out the epidemic of metaphors and similes that so mark his work. Here, Mr Carey turns in a bravura performance. Drawing on his great knowledge of poetry, he is able to show how literature outsmarts other art forms; how it alone is able to criticise itself, which makes it more powerful and self-aware than other forms; how only literature can comment, and therefore moralise, not by making you more moral but by giving you ideas to think with; and how by hinting rather than spelling out, it is literature's indistinctness that empowers the reader's imagination.

Read every word of Mr Kimmelman for ideas to think with, and start Mr Carey's book on page 171. You won't regret it.

The Accidental Masterpiece: On the Art of Life and Vice Versa.
By Michael Kimmelman.
Penguin; 224 pages; $24.95

By John Carey.
Faber and Faber; 304 pages; £12.99. To be published in America by Oxford University Press in December; $25

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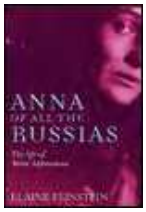
Anna Akhmatova

Lady in red

Aug 11th 2005
From The Economist print edition

Anna of All the Russias: A Life of Anna Akhmatova
By Elaine Feinstein



Orion; 322 pages; $28.95 and £20

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THE extraordinary misery of her life and the extraordinary merits of her poems make Anna Akhmatova one of the great literary figures of modern times. Elaine Feinstein's comprehensive and accessible biography evokes contradictory pity and gratitude in the reader. The pity makes one wish that Akhmatova's life had been easier. If only she had had one nice man in her life (her friendship with Isaiah Berlin aside), instead of many horrible ones. If only she had emigrated before the revolution. If only she had enjoyed better health. If only Soviet Russia had not been run by monsters who persecuted genius.

But then gratitude kicks in. It is through Akhmatova's eyes, queuing at the prison gate in the hope of handing in a food parcel to her imprisoned son, that we read the finest poetic depiction of the horrors of Stalinism. Other poems convey with great immediacy, even to a reader in the far away comfortable world many decades later, the stings of betrayal, and the aches of frustration and isolation that marked her life. It was her suffering, perhaps, that fuelled her genius.

It requires considerable self-confidence for a biographer to use their own translations of some of the world's best poems. Ms Feinstein is better placed than most: she is a poet and knows Russian. Some may quibble with her renderings, but they bring across the bony, spare quality of the original Russian.

> Your heart must have no earthly consolation.
> You must not cling to either wife or home.
> Take the bread out of your own child's mouth
> and give it to a man you do not know.
> You must be the most humble servant
> of the man who was your desperate enemy
> and call the forest beast your brother.
> Above all, never ask God for anything.

Akhmatova's lack of earthly consolation is well told: the poverty in which she often lived; her exceptionally unhappy love life; her tortured relationship, both obsessive and neglectful, with her son Lev; and her professional humiliation by the bureaucrats of the Soviet literary establishment. In the face of all that, she displayed both saintly stoicism and loyalty to her country. The path to exile trodden by Vladimir Nabokov, and later by Joseph Brodsky and Alexander Solzhenitsyn, was not for her.

But Ms Feinstein is also unsparing in describing the unhappiness she inflicted on other people, particularly on her lovers' wives. She details vividly Akhmatova's fecklessness and impracticality (not crimes, particularly in a poet, but still remarkable), as well as her generosity. However, she skates over the unhappiest episode in her subject's life: a bunch of poems written in 1950 which implicitly praised Stalin. That was done in the hope of winning her son's freedom from prison. But it deserves more than a paragraph. The poems themselves may have been mediocre, but it is wrong to describe them, as Ms Feinstein does, as “not remarkable”.

The feuds of the Russian literary intelligentsia are legendary. Some of the fiercest involved Akhmatova, and Ms Feinstein succeeds in being fair and explaining them comprehensibly. She also brings to life Akhmatova's contemporaries, particularly Marina Tsvetaeva, a poet whose life is equally tragic and whose work is perhaps even greater, though almost inaccessible to non-Russophones.

Compared with Akhmatova's verse, any prose style is bound to seem clunky, every judgment askew,

every insight incomplete. But it is hardly Ms Feinstein's fault that her biography is less inspired than her subject's poems.

Anna of All the Russias: A Life of Anna Akhmatova.
By Elaine Feinstein.
Orion; 322 pages; $28.95 and £20

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Arabs and the West

Ours to reason why

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THIS could have been a very good book: a searing attack on the glib endorsements of globalisation and facile analyses of history and culture offered, in Mark LeVine's un-humble opinion, by Thomas Friedman, Francis Fukuyama and Samuel Huntington—three bestselling luminaries who together form an “axis of arrogance and ignorance”. Instead, the book is over-long, over-ambitious and, given the expertise of Mr LeVine, an Arabic-speaking professor on the Irvine campus of the University of California, strangely naive.

But have patience (and forget the misleading title with its allusion to George Bush's suggestion that Islamist terrorists “hate us for our freedoms”): much of what Mr LeVine writes is worth reading. His underlying thesis is that globalisation is a form of corporate imperialism that, far from benefiting developing countries with extra wealth through extra trade, perversely widens their social and economic disparities. So when Mr Friedman and others bemoan the failure of the Middle East and North Africa to increase economic growth by jumping on the globalisation bandwagon, they miss the point, says Mr LeVine: “Lack of growth in the region has been an important, if not primary reason for the relative lack of poverty.”

Why They Don't Hate Us: Lifting the Veil on the Axis of Evil
By Mark LeVine

Oneworld Publications; 456 pages; $27.50 and £16.99

Buy it at
Amazon.com
Amazon.co.uk

Whether the unemployed of Algiers, dreaming of illegal entry into France, see it that way is doubtful, but Mr LeVine supports his thesis with such a wealth of statistical detail that even the most gung-ho advocate of IMF and World Bank programmes must pause for thought. When the region's painful history of colonialism is added, along with the plight of the Palestinians and the chaos of Iraq, the Arab world's mistrust of the West becomes much more reasonable.

The trouble is that Mr LeVine gets carried away by his own enthusiasms. Conventional analysis is bad, and so he castigates the Arab authors of the UN's Arab Human Development Report for noting that as many books are translated into Spanish each year as have been translated into Arabic in recorded history—but he does so on the basis that educated Arabs often read books in their original English, French or Spanish. So what? The point he glosses over is that there are far too many uneducated, indeed illiterate, Arabs.

Mr LeVine's pet enthusiasm is the notion that all can be resolved by what he calls “culture jamming” between scholars, activists and artists. That may work for music (the professor is an accomplished guitarist who has “jammed” with fellow musicians throughout the region) but does he really believe that this might hold back the forces of globalisation?

It would be wrong to say that the anti-globalisation movement (witness the Seattle demonstrations and the “anti-Davos” World Social Forum) has had no impact, but the effect has been not nearly as great as Mr LeVine imagines. The wise reader will forget the jamming and skip over the history of “the global peace and justice movement”. Instead, concentrate on what Mr LeVine says about the region's culture—and read the informative footnotes.

By Mark LeVine.
Oneworld Publications; 456 pages; $27.50 and £16.99

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Dirty words

Wash your mouth out

Aug 11th 2005
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AISCHROLATREIAN dictionaries, which glory in the meanings of naughty words, have been around for some time. But words used to talk about sex present problems for etymologists. First, most of the good ones are coined in private and so are deliberately hard for outsiders to understand. Second, there is usually an unknowable delay between when a word is first shouted across a bar and when it is written down, making its origin doubly mysterious.

Like the rest of the English language, many dirty words can be traced back through Latin and Greek to a common Indo-European root. A second infusion of surprisingly catchy ones came via the Vikings, who gave English some of its best ways to curse. One of the most common probably derives from the same root as the Norwegian word *fukka* and the Swedish *focka* (to copulate), and was first recorded in the early 16th century.

Dirty Words: The Story of Sex Talk
By Mark Morton

Atlantic; 368 pages; £12.99

Buy it at
Amazon.co.uk

Largely thanks to Chaucer, whose poetry is full of naughtiness, some of the best-sounding words come from old English. Some, like *swonken* (the past participle of *swink*, meaning “to toil”, but also used to mean *coupling*), have disappeared. Others, like *chode* (a *schlong* or penis) are now enjoying a revival. Sadly, Mr Morton does not offer a theory as to why some words are current, while others have withered.

New sex words are often spawned by innovations in other fields. From 1591 to 1603, for example, ten new words to denote a man who has sex with another man appeared, probably thanks to the comedies of the late-Elizabethan stage. Much later, *uranist* lost out to *homosexual* as a way to describe a *baedling*. Technology has left its mark too: in the 1970s, some prostitutes used *78* as slang for a client whose efforts were shortlived—a reference to the faster speed and shorter playtime of those records.

By Mark Morton.
Atlantic; 368 pages; £12.99

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French history

Au contraire

Aug 11th 2005
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WHY are the French so, well, French? Several recent English-language books have put the Gallic nation under the microscope, from the polemical ("Our Oldest Enemy" by John J. Miller and Mark Molesky; "The Arrogance of the French" by Richard Z. Chesnoff) to the fictional ("A Year in the Merde" by Stephen Clarke). Here, instead, is a serious history of modern France, which tries to unpack a complicated people through the forces that shaped them during the 20th century.

La Vie en Bleu: France and the French since 1900
By Rod Kedward

Penguin/Allen Lane; 740 pages; £30. To be published in America by Overlook Press in January 2006; $35

Buy it at Amazon.co.uk

Rod Kedward, a British historian, divides the period he has chosen into three, each part characterised by an underlying preoccupation. 1900-1931 is the era of the "primacy of the republic", when ideas about France's universalist message, its faith in reason and civilisation, and its secular anti-clericalism were entrenched. The 1920s-1969 marks the "spiral of ideology", when the aftermath of the Great Depression marked an intensified and highly contested quest for alternative ideals, from communism and socialism to fascism. The 1960s-2000s covers the "obsession with identity", an era when France tries to find a place in a globalising, post-colonial, post-ideological world.

The strength of this sympathetic and elegantly written book is Mr Kedward's refusal to over-simplify. At each turn, he manages to convey the conflict and antagonism that propel events. De Gaulle's struggle to impose himself in allied eyes as the legitimate resistance leader; collaboration with Vichy and the subsequent purges after liberation in 1944; the eventual denunciation by French Marxists of Stalin after 1956: each was fiercely contested. His account of de Gaulle's creation of a provisional government in Algiers in 1944 is typical: "In retrospect it seemed an evolutionary process. In reality it was one of fractures and disputes."

The author is particularly good on his speciality, the Vichy period: its iconography, the cult of Pétain and what he calls the "collective pathology" of a nation after the fall of France to Hitler. Given contemporary France's struggle to deal with the chill winds of globalisation—which partly motivated the electorate to reject the European Union constitution earlier this year—Mr Kedward's account of the political battles on the left over anti-capitalist ideology is also a useful reminder.

A splintered left characterises France throughout the century. The Communist Party was still regularly polling a quarter of the vote into the 1960s, dwarfing the Socialists in the 1969 presidential election. After May 1968, Marxist splinter groups, formed after disillusion with the Communists' Stalinist ties, argued that the French at the barricades were at the same point as the Russians in 1905: true revolution was just round the corner. Arlette Laguiller, who proposed a Trotskyist revolutionary programme at the 1974 presidential election, is still a political figure today. And the Socialist Party is still debating whether to ally itself to others further to the left.

Where others see only paradox in French history, Mr Kedward identifies a certain coherence. It is no contradiction, he argues, that "a political culture which extols the rational, orderly mind should also value the power of dissent so highly" since "it stems from an all-pervading involvement in disputing the conflictual merits of 'for' and 'against'."

However, despite his efforts to explain contradictions neatly, Mr Kedward's story in some ways gets lost in its complexity. He sets out to convey a "narrative", or rather multiple narratives, a word he has a particular fondness for. His evocation of a France composed of so many different strands leaves the reader at the end feeling faintly cheated of an over-arching theme. Apart, that is, from a theme of contradiction and conflict. Ah, Mr Kedward might reply, but that is France.

La Vie en Bleu: France and the French since 1900.
By Rod Kedward.
Penguin/Allen Lane; 740 pages; £30. To be published in America by Overlook Press in January 2006; $35

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Economist.com PRINT EDITION BOOKS AND ARTS
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South Africa's Constitution Hill

Making the cell walls talk

Aug 11th 2005 | JOHANNESBURG
From The Economist print edition

The transformation of an infamous prison into a beacon of hope

A dark place that is now shedding light

EVERY day, Joyce Seroke goes back to jail. She walks through the same entrance, past the same garden into the same atrium where, in 1976, she was stripped of her identity, and given a number. But instead of going to the cell where she was kept in solitary confinement for six months, the former anti-apartheid activist marches through the old prison to her office at the Commission for Gender Equality (CGE).

On August 9th the Johannesburg Women's Jail—once a symbol of apartheid oppression—reopened its doors as a museum. The conversion of the women's prison is part of the continuing development of Constitution Hill, a complex created on the site of an infamous prison-fort built in 1892 and closed down in 1983. The idea is to turn the jail—which detained the likes of Nelson Mandela, his former wife Winnie and the young Gandhi—into a “campus” devoted to constitutional rights.

Most of the prison buildings have been turned into museums, but some sections have been demolished to make way for South Africa's Constitutional Court, a modern construction of brick, wood and glass. The complex also provides space for the offices of constitutional watchdogs such as the CGE. A hotel, apartment buildings and shops are being planned.

South Africans like the irony of the court—which upholds one of the most progressive constitutions in the world—being created on the site of a prison whose raison d'être was the preservation of an unjust and brutal system. As a reminder of the suffering on which South Africa's democracy has been built, bricks from some of the prison buildings were used to erect the new court. Lectures and debates are regularly organised in the prison yards.

Turned into a museum, the prison cells tell tales of human tragedy, driving home the minutiae of life behind bars. The inmates, and the wardens too, were subject to different regimens, depending on the colour of their skin. White inmates did not have it easy by any means, but they were granted more space and better food than their black counterparts.

As interviews with former prisoners are projected on to the cell walls, much sadness is depicted: the violence of communal cells, the strict hierarchy of prison life, and the sadistic and systematic humiliations. The display of paper-thin mats and rationed blankets, torture trestles and batons give an idea of the material conditions the prisoners suffered. Stories of solidarity also emerge. A makeshift birthday card, preserved for 30 years, allows Jeannie Noel, a former political prisoner, to recall how depressed she felt on her birthday until the women in her unit burst into her cell wearing nighties and

singing.

The jail also conjures up the broader picture of women under apartheid, their precarious life and their contribution to the regime's demise. “Every woman I know in Johannesburg has been incarcerated in this jail,” says Ms Seroke.

A shopping bag is on display, as a reminder that black women without a pass were routinely arrested, sometimes with babies on their backs, while trying to buy food in white city-centres. “My grandmother had taught me to say goodbye every time we left home,” explains Nolundi Ntamo, arrested in 1980, “because we never knew if we would come back or not.” Being in love with a white man also guaranteed a trip to the jail.

A wedding dress hangs in a solitary cell. It belongs to Nikiwe Deborah Matshoba, a political activist who was banned from attending her own wedding. She was detained at the same time as her husband, leaving their one-year-old son without parents. Winnie Mandela was pregnant when she was first incarcerated here. “I was visited by my children in the same prison 18 years later in 1976—the very daughter that I had been expecting when I was in that prison for the first time—in pursuit of the same ideals,” she remembers.

Many of the women who had passed through these walls were keen to help turn the jail into what has become the country's only memorial to their suffering and struggle. “I want people to see that beautiful 22-year-old who came into this cell and stood for what she believed in,” explains Mali Mokoena. “That was me.” But the project has not been without controversy, as some former inmates feel that the addition of modern buildings and the facelift of the old prison soften the dark reality. “At the beginning, I felt the same way,” admits Ms Seroke. “But I have reached closure, and I look at this place as a beacon of hope.”

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Economist.com PRINT EDITION OBITUARY
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Obituary

Robin Cook

Aug 11th 2005
From The Economist print edition

Reuters

Robert Finlayson (Robin) Cook, politician and parliamentarian, died on August 6th, aged 59

ON MARCH 18th this year, Robin Cook—former leader of the House of Commons, former foreign secretary, MP for Livingston—wrote a column for the *Guardian*. It concluded: "I am on Bongo Fury for the County Hurdle getting-out stakes, but given my luck so far this week you may want to treat that as a warning rather than a tip."

Mr Cook did not disguise his passion for the turf. He studied form avidly, wrote a tipster's column for the *Glasgow Herald*, and not long before he died—suddenly, from a heart attack while hill-walking in the Scottish Highlands—fronted a consortium to bid for the *Racing Post*. Nor did he disguise why he liked horse-racing. Beyond its obvious thrills, it was a social equaliser. All classes came out in all weathers to enjoy it, and he, a government minister, was no more likely to win money at the course than anybody else.

This joyous proletarianism showed that Old Labour was Mr Cook's natural home. So did the faintly evil reddish beard, the loud tweed jackets and his fierce opposition to any part-privatisation of the National Health Service. He burned to establish a new centre-left agenda based on "fairness" and "equality", and mourned the loss of "social cohesion" in Britain. Time and again, he found Tony Blair's newly garbed party sadly disappointing for its lack of radical fire.

His own route to politics was a rough-and-tumble Scottish one: from a Lanarkshire council estate, via socialist reading at school, through a left-wing takeover of Edinburgh city council, through a rambunctious campaign for Edinburgh North in 1970 in which he pilloried the Earl of Dalkeith, the Tory candidate, by sending round snaps of the earl on horseback. He arrived in Westminster in 1974 with formidable debating skills, but also with a reputation for being unruly and rude.

This meant that though his rise was steady, from shadow health secretary in 1989 to shadow trade and industry in 1992 to shadow foreign secretary in 1994 (in which he savaged John Major's government over the findings of the Scott report into arms to Iraq), he was always something of an outsider. He never stood a chance of dislodging Gordon Brown from the chancellor's slot, which he wanted, let alone of leading the party, though his was possibly the most searching brain in it.

For one thing, he was not good-looking enough. He was once described as “yon wee pixie” by a Scottish Tory MP, and rather liked it, as well as all the unkind references to strutting cock-bantams and garden gnomes. Even his two terriers, Tammy and Tasker, were lovingly described as too badly behaved to be New Labour dogs.

Mr Cook was also that dangerous commodity, a passionate man in a party that now demanded discipline and was obsessed by its day-to-day coverage in the press. He cared for neither, believing that even ministers should “throw away their pagers and speak from the heart”. His stint as foreign secretary proper after 1997 was typically nerve-wracking. He announced, to much ribbing, an “ethical foreign policy”, only to find that British policy around the globe was being determined by weapons contracts. He irritated Israel by visiting an illegal settlement, and annoyed both India and Pakistan, a rare feat, by offering to sort out Kashmir.

Just before all that, he was discovered by the *News of the World* to be having an affair with his secretary and had to be ordered by Alastair Campbell, Mr Blair's spinmaster, to put some “clarity” into his personal life. Clarity consisted of leaving his wife and marrying his mistress; his wife responded, incandescently, with stories of more mistresses and a whisky problem. To no one's great surprise, Mr Cook was replaced in 2001 by the very much safer Jack Straw, and was appointed to be leader of the Commons.

A standing ovation

This demotion, as he saw it, turned out to be the making of him. For Mr Cook cared, above all else, about making Parliament work for the modern age. He agonised over the disengagement of the British public from politics, and the reduction of government to an adversarial soap opera in which the voters had no stake. Now he was in charge of managing the Commons and, for good measure, pushing through Labour's plans to transform the House of Lords from an hereditary to a representative chamber.

His work was frustrated by Mr Blair, who not only proposed to make the Lords appointed, rather than elected—thereby rendering impossible, in Mr Cook's view, the proper scrutiny of the executive by Parliament—but also increasingly intended to go to war with Iraq. This Mr Cook ardently opposed, convinced that “evangelical certainty”, rather than hard facts, had pushed a prime minister he admired into a hole he could not get out of.

In March 2003 he resigned from the government, with a speech so good that it was given the only standing ovation ever recorded in the Commons. MPs may have been startled, as much as anything, by the spectacle of a resignation on principle from the party of shift and spin. They may also have been impressed by how much Mr Cook had sacrificed to make his decision; for the first time in years, he had missed the Gold Cup at Cheltenham.

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Overview

Aug 11th 2005
From The Economist print edition

The **oil price** again reached a record high, briefly touching $65 a barrel this week due to fears of a terrorist attack in Saudi Arabia, potential trade sanctions on Iran and breakdowns at American refineries.

America's Federal Reserve raised short-term interest rates for its tenth consecutive meeting, to 3.5%. The Fed's decision seems to be supported by the increase in employment in America: 207,000 more jobs were added to the non-farm payroll in July, after having increased by 166,000 in the previous month. The unemployment rate remained at 5.0% in the same month.

Economic performance in the **euro area** is mixed. Germany's GDP was flat in the second quarter; its year-on-year growth rate slowed to 0.6%. However, Italy's GDP grew faster than expected in the same quarter, by an annual rate of 2.8%. Spain's GDP grew at an annual rate of 3.6%. French industrial production gained 0.3% in June, but fell by 0.4% compared with a year earlier.

More gloomy news from **Britain**: industrial output dropped by 1.9% in the year to June.

Japan's corporate-goods price index, a measure of wholesale prices, rose by 1.5% in the year to July, faster than expected. Private-sector machinery orders shot up by 11.1% in June, about twice what most analysts had predicted.

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Output, demand and jobs

Aug 11th 2005
From The Economist print edition

% change on year ago

	GDP			The Economist poll GDP forecasts		Industrial production		Retail sales (volume)		Unemployment % rate		
	latest		qtr*	2005	2006	latest		latest		latest		year ago
Australia	+ 1.9	Q1	+ 2.8	+ 2.3	+ 3.1	+ 1.2	Q1	+ 1.6	Q2	5.0	Jul	5.7
Austria	+ 2.0	Q1	+ 0.8	+ 1.9	+ 2.0	+ 5.6	May	+ 3.8	May	5.1	Jul	4.9
Belgium	+ 1.4	Q2	+ 1.2	+ 1.2	+ 1.9	+ 1.1	May	+ 4.3	May	13.4	Jul†	12.8
Britain	+ 1.7	Q2	+ 1.5	+ 2.1	+ 2.1	– 1.9	Jun	+ 1.7	Jun	4.8	May††	4.8
Canada	+ 3.3	Q1	+ 2.3	+ 2.7	+ 3.0	+ 1.8	May	+ 5.6	May	6.8	Jul	7.1
Denmark	+ 0.8	Q1	+ 0.6	+ 2.0	+ 2.2	+ 2.0	May	+ 7.6	Jun	5.8	Jun	6.5
France	+ 1.8	Q1	+ 1.4	+ 1.5	+ 1.9	– 0.4	Jun	+ 0.8	Jun	10.1	Jun	10.0
Germany	+ 0.6	Q2	nil	+ 1.1	+ 1.3	+ 2.8	Jun	+ 1.9	Jun	11.6	Jul§	10.6
Italy	+ 0.1	Q2	+ 2.8	– 0.1	+ 1.2	– 3.0	Jun	– 0.3	May	7.8	Mar	8.2
Japan	+ 1.3	Q1	+ 4.9	+ 1.7	+ 1.7	+ 0.1	Jun	+ 3.1	Jun	4.2	Jun	4.6
Netherlands	+ 1.3	Q2	+ 4.9	+ 0.4	+ 1.5	– 0.1	Jun	– 2.8	Apr	6.7	Jun**	6.4
Spain	+ 3.4	Q2	+ 3.6	+ 3.1	+ 2.8	– 0.2	Jun	+ 1.4	Jun	9.8	Jun	11.1
Sweden	+ 2.2	Q2	+ 2.4	+ 1.9	+ 2.6	– 0.9	May	+ 9.6	Jun	7.1	Jun†	5.8
Switzerland	+ 0.8	Q1	+ 0.2	+ 0.8	+ 1.5	– 0.3	Q1	– 0.4	May	3.5	Jul†	3.6
United States	+ 3.6	Q2	+ 3.4	+ 3.6	+ 3.3	+ 3.9	Jun	+ 7.6	Jun	5.0	Jul	5.5
Euro area	+ 1.4	Q1	+ 1.9	+ 1.3	+ 1.7	+ 0.1	May	+ 0.9	Jun	8.7	Jun	8.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 2.0	Q1	+ 0.5	na	na	– 9.8	Jun	+ 6.3	May	8.7	Jun†	8.9
Greece	+ 3.5	Q2	na	na	na	– 2.3	Jun	+ 5.3	May	9.9	Mar	10.8
Iceland	+ 2.9	Q1	na	na	na	na		na		2.2	May†	3.3
Ireland	+ 2.4	Q1	+ 1.0	na	na	– 3.4	May	+ 4.6	May	4.3	Jul	4.4
Luxembourg	+ 3.1	Q1	na	na	na	+ 4.6	Apr	– 1.8	Jun	4.4	Jun	3.9
New Zealand	+ 1.9	Q1	+ 1.5	na	na	+ 3.5	Q4	+ 5.8	Q1	3.7	Q2	4.0
Norway	– 0.8	Q1	+ 2.2	na	na	– 2.7	Jun	+ 3.7	Jun	4.7	Jun**	4.5
Portugal	+ 0.1	Q1	+ 0.8	na	na	+ 1.2	Jun	+ 6.6	Jun	7.5	Q1†	6.4

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Mar-May; claimant count rate 2.8% in Jun.
§EU harmonised rate 9.2% in Jun. **Apr-Jun.

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Prices and wages

Aug 11th 2005
From The Economist print edition

% change on year ago

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2005	2006	latest		year ago	latest		year ago
Australia	+ 2.5	Q2	+ 2.5	+ 2.7	+ 2.6	+ 6.9	Q2	+ 2.8	+ 4.5	Q1	+ 5.0
Austria	+ 2.3	Jun	+ 2.3	+ 2.1	+ 1.7	+ 1.1	Jul	+ 6.0	+ 2.2	Jun	+ 2.2
Belgium	+ 3.1	Jul	+ 2.4	+ 2.3	+ 1.8	+ 2.2	Jun	+ 4.2	+ 2.6	Apr	+ 2.3
Britain	+ 2.0	Jun*	+ 1.6	+ 1.9	+ 1.9	+ 3.0	Jul	+ 2.6	+ 4.1	May†	+ 4.6
Canada	+ 1.7	Jun	+ 2.5	+ 2.1	+ 2.2	+ 0.2	Jun	+ 7.0	+ 1.1	May	+ 3.9
Denmark	+ 2.0	Jul	+ 1.3	+ 1.5	+ 1.7	+ 3.9	Jun	+ 2.4	+ 3.1	Q1	+ 3.3
France	+ 1.7	Jun	+ 2.4	+ 1.8	+ 1.5	+ 2.9	Jun	+ 2.2	+ 2.9	Q1	+ 2.8
Germany	+ 2.0	Jul	+ 1.8	+ 1.6	+ 1.3	+ 2.5	Jul	+ 3.9	+ 0.6	May	+ 1.9
Italy	+ 2.1	Jul	+ 2.3	+ 2.1	+ 1.9	+ 3.7	Jun	+ 3.2	+ 3.0	Jun	+ 3.3
Japan	– 0.5	Jun	nil	– 0.1	+ 0.3	+ 1.5	Jul	+ 1.7	– 0.1	Jun	+ 1.8
Netherlands	+ 1.6	Jul	+ 1.1	+ 1.4	na	+ 4.9	Jun	+ 3.6	+ 0.6	Jun	+ 1.4
Spain	+ 3.3	Jul	+ 3.4	+ 3.1	+ 2.8	+ 4.4	Jun	+ 4.0	+ 2.5	Q1	+ 3.2
Sweden	+ 0.3	Jul	+ 0.7	+ 0.5	+ 1.3	+ 3.2	Jun	+ 1.5	+ 1.1	May	+ 3.1
Switzerland	+ 1.2	Jul	+ 0.9	+ 1.1	+ 1.1	+ 0.5	Jun	+ 1.5	+ 0.9	2004	+ 1.4
United States	+ 2.5	Jun	+ 3.3	+ 2.9	+ 2.6	+ 3.6	Jun	+ 4.3	+ 2.7	Jul	+ 2.0
Euro area	+ 2.2	Jul	+ 2.3	+ 2.0	+ 1.6	+ 4.3	Jun	+ 2.4	+ 3.1	Q1	+ 3.0
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.1	Jun	– 0.1	na	na	+ 4.0	Jun	+ 1.0	+ 4.1	Q1	+ 4.2
Greece	+ 3.9	Jul	+ 2.9	na	na	+ 5.0	Jun	+ 4.8	na		na
Iceland	+ 3.5	Jul	+ 3.6	na	na	+ 3.7	Jul	+ 5.3	+ 6.3	Jun	+ 5.1
Ireland	+ 2.1	Jun	+ 2.3	na	na	– 0.3	Jun	+ 1.3	+ 6.4	Q1	+ 3.9
Luxembourg	+ 2.2	Jun	+ 2.6	na	na	+ 6.7	May	+ 7.7	+ 0.4	May	+ 2.4
New Zealand	+ 2.8	Q2	+ 2.4	na	na	+ 4.2	Q1	– 0.6	+ 2.5	Q1	+ 2.2
Norway	+ 1.4	Jul	+ 1.5	na	na	+19.3	Jul	+13.9	+ 3.7	Q1	+ 3.5
Portugal	+ 1.6	Jun	+ 2.7	na	na	+ 3.7	Jun	+ 2.3	– 3.0	May	+ 0.8

*RPI inflation rate 2.9% in Jun. †Mar-May.

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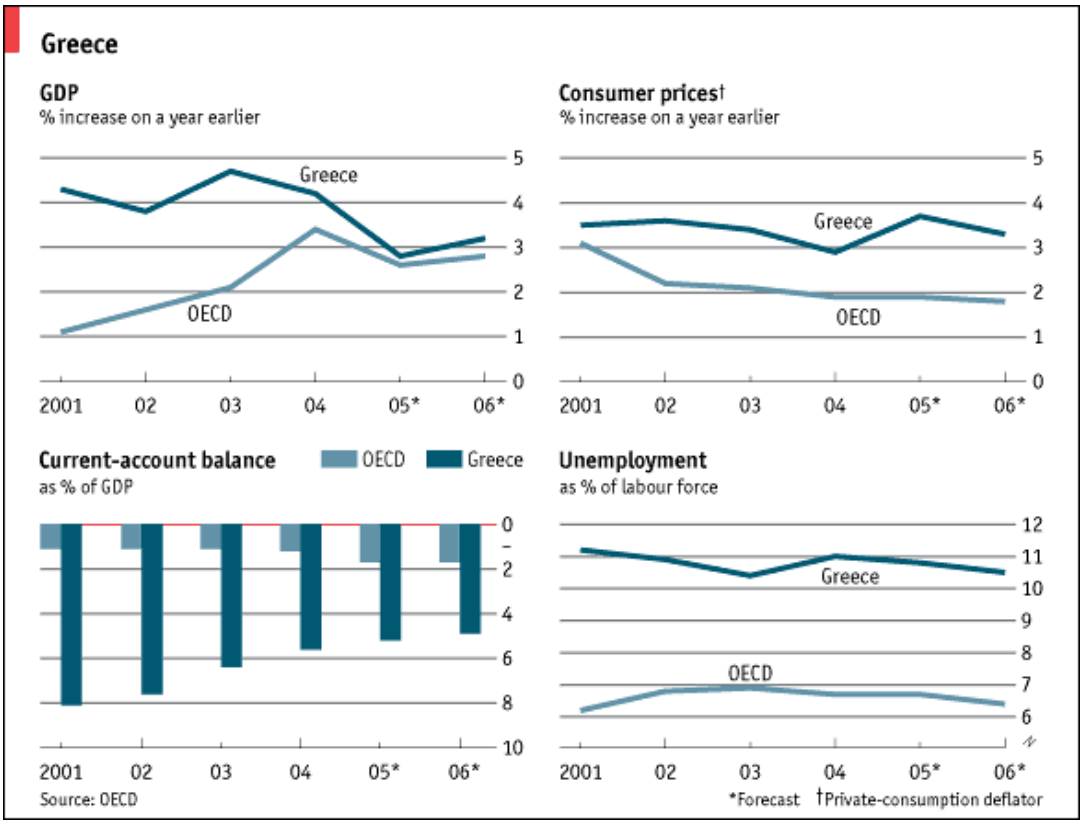
Greece

Aug 11th 2005
From The Economist print edition



The Greek economy grew briskly in the past four years, performing far better than the OECD average, according to the organisation's latest survey of the country. But unemployment and inflation remain stubbornly high, and income per head still lags behind the rest of the euro area. The current account also remains deeply in deficit. Living standards would rise more quickly, the OECD argues, if the government reformed product markets, to promote competition, and labour markets, to make wages more flexible. The government's immediate priority, however, should be to reduce its budget deficit, which stood at 6% of GDP in 2004. This is important not only to meet the fiscal rules of the euro zone, but also to prepare for the growing burden of an ageing population. The OECD predicts that GDP growth will slow to 2.8% this year, but quicken to 3.2% next year.

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Money and interest rates

Aug 11th 2005
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Aug 10th 2005)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+ 5.3	+10.6	Jun	5.63	5.45	5.16	5.33	5.65	6.34
Britain	+ 3.8	+11.0	Jun	4.53	4.91	4.26	4.39	4.98	5.19
Canada	+ 8.4	+10.4	Jun	2.60	2.05	3.17	4.08	4.67	5.25
Denmark	+21.3	+16.8	Jun	2.20	2.25	2.23	3.32	4.19	4.95
Japan	+ 4.4	+ 1.7	Jul	0.02	0.03	0.15	1.44	1.67	1.52
Sweden	+ 1.8	+ 9.4	Jun	1.48	1.99	2.06	3.17	4.34	2.90
Switzerland	– 2.5	+ 4.7	Jun	0.76	0.52	1.06	2.01	2.62	2.04
United States	+ 2.1	+ 4.8	Jun	3.74	1.63	4.11	4.39	4.28	5.26
Euro area†	+10.5	+ 7.5	Jun	2.13	2.11	2.29	3.31	4.05	3.55

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. Benchmarks: US 30-year 4.58%, Japan No. 270 1.44%. Central bank rates: US fed funds 3.50%, ECB refinancing 2.00%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Aug 11th 2005
From The Economist print edition

2000=100

	Aug 2nd	Aug 9th*	% change on one month	% change on one year
Dollar index				
All items	136.9	133.6	– 1.4	+ 8.2
Food	130.2	126.5	– 2.5	+ 6.6
Industrials				
All	145.4	142.7	– 0.1	+10.0
Nfa†	135.0	133.1	– 2.5	– 0.3
Metals	151.1	147.9	+ 1.0	+15.9
Sterling index				
All items	117.2	113.5	– 2.0	+11.5
Euro index				
All items	103.7	100.0	– 2.6	+ 7.9
Yen index				
All items	141.4	138.9	– 0.4	+ 9.4
Gold				
$ per oz	432.65	433.70	+ 1.7	+ 8.4
West Texas Intermediate				
$ per barrel	61.89	63.10	+ 4.2	+41.8

* Provisional. † Non-food agriculturals.

Our commodity-price index was rebased in February 2005.

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Stockmarkets

Aug 11th 2005
From The Economist print edition

Market indices

	Aug 10th	2005 high	2005 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,384.8	4,384.8	3,905.5	+ 1.4	nil	+ 8.2	+ 5.5
Austria (ATX)	3,260.7	3,260.7	2,415.0	+ 1.8	nil	+34.1	+22.2
Belgium (Bel 20)	3,314.8	3,314.8	2,958.8	+ 1.4	-10.0	+13.0	+ 3.0
Britain (FTSE 100)	5,377.5	5,377.5	4,783.6	+ 0.8	-22.4	+11.7	+ 4.5
Canada (Toronto Composite)	10,671.4	10,671.4	9,006.2	+ 0.7	- 6.3	+15.4	+14.1
Denmark (KBX)	330.1	332.7	257.8	+ 1.6	- 0.8	+28.1	+16.3
France (SBF 250)	3,146.1	3,146.1	2,633.6	+ 0.7	-28.3	+19.4	+ 8.8
(CAC 40)	4,527.1	4,527.1	3,816.1	+ 0.7	-34.6	+18.5	+ 7.9
Germany (DAX)*	4,990.6	4,990.6	4,178.1	+ 1.4	-38.1	+17.3	+ 6.8
Italy (S&P/MIB)	34,027.0	34,027.0	30,645.0	+ 0.4	-32.1	+10.1	+ 0.3
Japan (Nikkei 225)	12,098.1	12,098.1	10,825.4	+ 1.0	-68.9	+ 5.3	- 2.3
(Topix)	1,227.9	1,227.9	1,109.2	+ 1.3	-57.4	+ 6.8	- 1.0
Netherlands (AEX)	401.6	401.6	347.0	+ 1.2	-42.8	+15.4	+ 5.1
Spain (Madrid SE)	1,103.7	1,103.7	950.9	+ 0.8	- 3.7	+15.1	+ 4.9
Sweden (Affarsvarlden Gen)	263.6	263.6	218.9	+ 0.6	-34.2	+19.1	+ 5.0
Switzerland (Swiss Market)	6,689.2	6,689.2	5,669.6	+ 0.5	-20.5	+17.5	+ 6.3
United States (DJIA)	10,594.4	10,940.6	10,012.4	- 1.0	- 9.6	- 1.7	- 1.7
(S&P 500)	1,229.1	1,245.0	1,137.5	- 1.3	-19.5	+ 1.4	+ 1.4
(NASDAQ Comp)	2,157.8	2,218.2	1,904.2	- 2.7	-57.3	- 0.8	- 0.8
Europe (FTSEurofirst 300)†	1,199.9	1,199.9	1,038.6	+ 1.1	-29.6	+15.2	+ 4.9
Euro area (FTSE Euro 100)†	1,026.7	1,026.7	894.4	+ 0.9	-33.8	+14.0	+ 3.8
World (MSCI)‡	1,203.6	1,204.7	1,115.0	- 0.1	-16.9	+ 2.9	+ 2.9
World bond market (Citigroup)††	638.9	662.3	626.9	+ 0.2	- 3.5	- 4.1	- 4.1

*Total return index. †In euro terms. ‡Morgan Stanley Capital International index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Aug 11th 2005
From The Economist print edition

	Trade balance*, $bn latest 12 months	Current-account balance $bn latest 12 mths	Current-account balance The Economist poll % of GDP, forecast 2005	Current-account balance The Economist poll % of GDP, forecast 2006	Exchange rate trade-weighted† 2000=100 Aug 10th	Exchange rate trade-weighted† 2000=100 year ago	Currency units per $ Aug 10th	Currency units per $ year ago	Currency units per £	Currency units per euro	Currency units per ¥100	Budget balance % of GDP 2005‡
Australia	− 17.7 Jun	− 42.4 Q1	− 5.9	− 5.6	117.5	110.7	1.31	1.40	2.35	1.62	1.18	+ 0.9
Austria	− 1.6 May	+ 0.5 May	− 0.3	− 0.3	103.7§	103.8	0.81	0.82	1.45	–	0.73	− 2.0
Belgium	+ 16.5 May	+ 12.2 Mar	+ 2.9	+ 2.8	104.1§	104.2	0.81	0.82	1.45	–	0.73	− 0.5
Britain	−111.2 Jun	− 44.0 Q1	− 2.5	− 2.6	98.6	101.9	0.56	0.55	–	0.69	0.50	− 2.9
Canada	+ 47.5 May	+ 20.2 Q1	+ 1.3	+ 1.2	118.9	108.9	1.21	1.33	2.18	1.50	1.10	+ 1.2
Denmark	+ 9.9 Jun	+ 10.8 Jun	+ 2.0	+ 1.8	106.0	106.0	6.03	6.09	10.8	7.46	5.45	+ 1.8
France	− 26.0 May	− 24.6 May	− 0.7	− 0.5	106.6§	106.8	0.81	0.82	1.45	–	0.73	− 3.0
Germany	+198.5 Jun	+108.5 Jun	+ 3.7	+ 3.5	104.3§	104.5	0.81	0.82	1.45	–	0.73	− 3.5
Italy	− 6.8 May	− 21.5 May	− 1.4	− 1.5	76.4§	76.5	0.81	0.82	1.45	–	0.73	− 4.4
Japan	+113.2 Jun	+166.1 Jun	+ 3.5	+ 3.4	86.0	86.2	110	111	199	137	–	− 6.1
Netherlands	+ 40.7 May	+ 33.9 Q1	+ 3.7	+ 3.6	103.5§	103.6	0.81	0.82	1.45	–	0.73	− 2.2
Spain	− 88.1 May	− 69.9 Apr	− 5.4	− 5.5	77.0§	77.1	0.81	0.82	1.45	–	0.73	+ 0.5
Sweden	+ 22.5 Jun	+ 29.7 Q1	+ 5.7	+ 5.2	96.4	97.6	7.54	7.54	13.6	9.34	6.83	+ 0.8
Switzerland	+ 7.3 Jun	+ 40.2 Q1	+11.2	+10.8	106.4	107.0	1.26	1.26	2.26	1.56	1.14	− 1.0
United States	−717.9 May	−717.0 Q1	− 6.3	− 6.2	85.0	87.4	–	–	1.80	1.24	0.91	− 4.1
Euro area	+ 63.5 May	+ 23.2 May	+ 0.4	+ 0.4	117.0	115.3	0.81	0.82	1.45	–	0.73	− 2.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 12.8 May	+ 6.5 May	na	na	81.2§	81.4	0.81	0.82	1.45	–	0.73	+ 1.3
Greece	− 33.7 May	− 15.7 May	na	na	59.7§	59.8	0.81	0.82	1.45	–	0.73	− 3.8
Iceland	− 0.9 Jun	− 1.4 Q1	na	na	105.7**	95.1	64.3	71.4	116	79.6	58.2	+ 1.1
Ireland	+ 40.9 May	− 3.1 Q1	na	na	93.6§	93.7	0.81	0.82	1.45	–	0.73	− 0.7
Luxembourg	− 4.4 May	+ 3.0 Q1	na	na	104.1§	104.2	0.81	0.82	1.45	–	0.73	− 0.8
New Zealand	− 3.5 Jun	− 7.0 Q1	na	na	135.4	129.4	1.44	1.53	2.59	1.78	1.30	+ 3.2
Norway	+ 40.4 Jun	+ 37.9 Q1	na	na	110.9	104.4	6.38	6.82	11.5	7.90	5.77	+ 14.4
Portugal	− 20.6 May	− 15.3 May	na	na	94.3**	93.3	0.81	0.82	1.45	–	0.73	− 5.3

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, June average. ‡OECD forecast. **IMF, April average.

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Small stockmarkets

Aug 11th 2005
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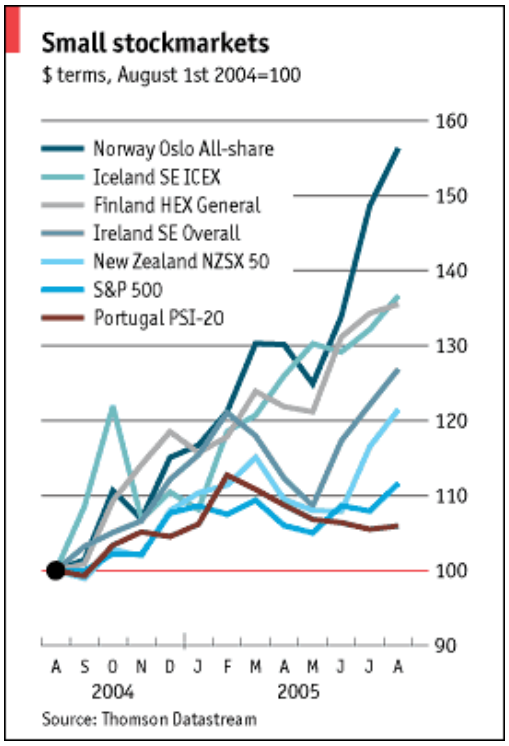

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Overview

Aug 11th 2005
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In the 12 months to June, industrial production rose by 5.9% in **Peru,** by 3.4% in **Malaysia** and by 1.6% in **Turkey**.

Singapore's GDP growth in the year to the second quarter was revised up to 5.2%.

China's trade surplus grew to $87.6 billion in the year to July, from $13.9 billion the previous year. Meanwhile **Taiwan's** trade surplus fell to $2.1 billion in the year to July from $12.7 billion a year earlier.

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Inflation rates

Aug 11th 2005
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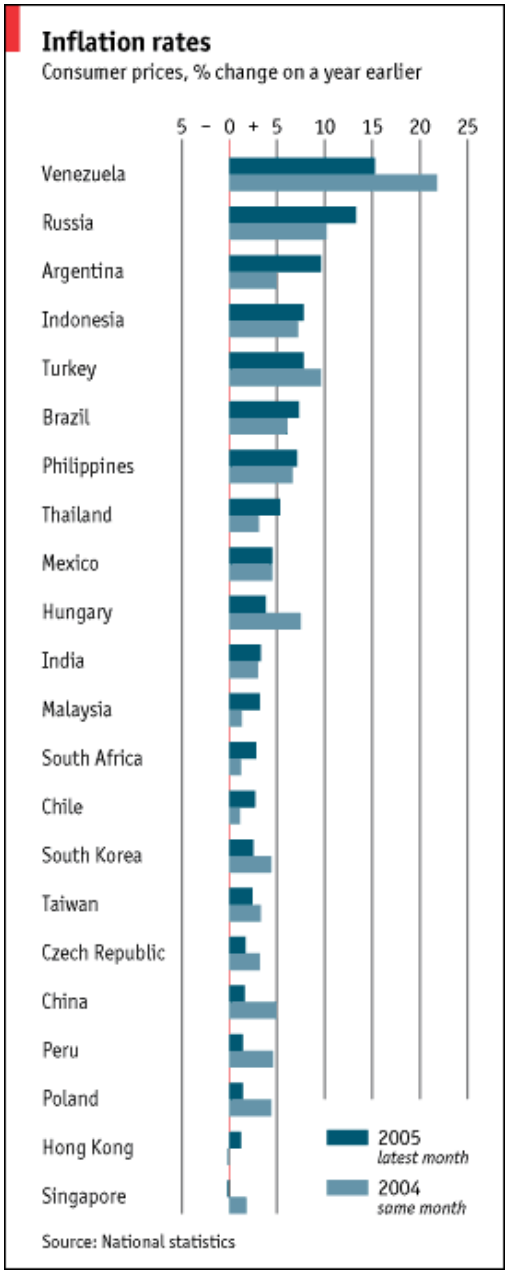
Inflation worries have eased over the past year in many emerging economies. In China, consumer-price inflation has fallen to 1.8% from 5.3% a year ago. Rising prices are still troublesome for Russia and Argentina, but they are now welcome in Hong Kong, which has struggled with deflation in the past. Singapore is not so lucky: its consumer prices fell by 0.2% over the past year.



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Economy

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	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.5	Q2	+16.8	Jun	+ 1.8	Jul	+87.6	Jul	+68.7	2004	711.0	Jun
Hong Kong	+ 6.0	Q1	– 0.6	Q1	+ 1.2	Jun	– 9.7	Jun	+18.5	Q1	121.9	Jul
India	+ 7.0	Q1	+10.8	May	+ 3.3	Jun	–32.4	Jun	– 6.4	Q1	130.1	Jul
Indonesia	+ 6.4	Q1	+10.1	Mar	+ 7.8	Jul	+27.4	Jun	+ 7.8	Q1	32.6	Jun
Malaysia	+ 5.7	Q1	+ 3.4	Jun	+ 3.2	Jun	+24.0	Jun	+16.7	Q1	74.5	Jun
Philippines	+ 4.6	Q1	+ 5.4	May	+ 7.1	Jul	– 0.1	May	+ 2.9	Mar	15.1	Jun
Singapore	+ 5.2	Q2	+11.1	Jun	– 0.2	Jun	+16.3	Jun	+29.2	Q1	116.3	Jul
South Korea	+ 3.3	Q2	+ 4.1	Jun	+ 2.5	Jul	+26.0	Jul	+23.2	Jun	204.1	Jun
Taiwan	+ 2.5	Q1	+ 1.3	Jun	+ 2.4	Jul	+ 2.1	Jul	+16.9	Q1	253.6	Jul
Thailand	+ 3.3	Q1	+ 8.8	Jun	+ 5.3	Jul	– 6.7	Jun	– 2.2	Jun	47.2	Jun
Argentina	+ 8.0	Q1	+ 2.0	Jun	+ 9.6	Jul	+11.0	Jun	+ 2.8	Q1	21.4	May
Brazil	+ 2.9	Q1	+ 5.5	May	+ 7.3	Jun	+39.9	Jul	+12.6	Jun	60.7	May
Chile	+ 5.7	Q1	+ 7.4	Jun	+ 2.7	Jun	+ 9.0	Jun	+ 1.1	Q1	16.6	Jun
Colombia	+ 3.6	Q1	+ 2.1	May	+ 4.9	Jul	+ 1.5	Apr	– 0.8	Q1	12.5	Jun
Mexico	+ 2.4	Q1	+ 3.0	May	+ 4.5	Jul	– 9.8	Jun	– 8.7	Q1	65.6	Jun
Peru	+ 7.1	May	+ 5.9	Jun	+ 1.4	Jul	+ 3.5	May	+ 0.4	Q1	14.5	Jul
Venezuela	+ 7.9	Q1	+28.2	Apr	+15.3	Jul	+22.6	Q1	+14.9	Q1	22.3	May
Egypt	+ 4.7	Q4	+ 3.3	2004†	+ 4.7	Jun	– 9.5	Q1	+ 4.4	Q1	17.6	Jun
Israel	+ 4.1	Q1	+ 5.2	May	+ 0.3	Jun	– 7.6	Jun	+ 1.9	Q1	24.5	Jul
South Africa	+ 4.2	Q1	+ 1.2	May	+ 2.8	Jun	– 2.1	Jun	– 8.5	Q1	17.2	Jul
Czech Republic	+ 4.4	Q1	+ 4.0	May	+ 1.7	Jul	+ 1.0	Jun	– 4.4	Q1	29.8	Jul
Hungary	+ 2.9	Q1	+10.1	May	+ 3.8	Jun	– 2.7	Q1	– 9.2	Q1	17.7	Jul
Poland	+ 2.1	Q1	+ 6.8	Jun	+ 1.4	Jun	– 3.6	May	– 1.0	May	39.8	Jun
Russia	+ 5.2	Q1	+ 6.9	Jun	+13.3	Jun	+108.6	Jun	+69.2	Q1	147.8	Jun
Turkey	+ 4.8	Q1	+ 1.6	Jun	+ 7.8	Jul	–38.3	Jun	–19.3	Jun	40.0	Jun
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+ 7.2	Q1	+11.1	Jun	+ 3.8	Jul	– 2.4	May	– 1.3	May	1.7	May
Latvia	+ 7.4	Q1	+ 9.9	May	+ 6.1	Jul	– 2.7	May	– 1.6	May	2.0	May
Lithuania	+ 8.2	Q2	na		+ 1.8	Jul	– 3.1	May	– 1.5	Q1	3.5	May
Slovakia	+ 5.1	Q1	+ 1.6	Jun	+ 2.5	Jun	– 2.1	May	– 2.0	Apr	15.7	May
Slovenia	+ 2.6	Q1	+ 1.0	Jun	+ 2.3	Jul	– 1.3	May	nil	May	8.4	Apr
Pakistan	+ 6.4	2004†	+13.6	Apr	+ 8.7	Jun	– 6.2	Jun	– 1.5	Q1	10.4	May
Saudi Arabia	+ 5.2	2004	na		+ 0.3	May	+84.9	2004	+51.5	2004	26.7	May

*Excluding gold, except Singapore; IMF definition. †Year ending June.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Aug 11th 2005
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	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Aug 10th		Dec 31st 2004	
	Aug 10th	year ago	Aug 10th	% a year		one week	in local currency	in $ terms
China	8.11	8.28	14.6	3.00	1,224.6	+5.2	– 7.9	– 6.0
Hong Kong	7.77	7.80	14.0	3.67	15,346.4	+1.5	+ 7.8	+ 7.9
India	43.5	46.3	78.2	5.47	7,729.8	–0.3	+ 17.1	+ 16.9
Indonesia	9,768	9,273	17,551	9.12	1,176.8	–1.3	+ 17.7	+ 11.8
Malaysia	3.75	3.80	6.73	2.88	939.5	–1.4	+ 3.5	+ 5.0
Philippines	55.8	55.7	100.3	7.00	2,010.4	+1.1	+ 10.3	+ 10.9
Singapore	1.65	1.71	2.96	2.00	2,338.5	–1.1	+ 13.2	+ 12.3
South Korea	1,016	1,155	1,825	3.50	1,104.9	–1.1	+ 23.3	+ 25.7
Taiwan	31.9	34.0	57.4	1.45	6,356.8	–1.5	+ 3.5	+ 2.8
Thailand	40.9	41.5	73.5	3.20	684.6	–0.5	+ 2.5	– 2.6
Argentina	2.87	3.03	5.16	6.75	1,509.2	+0.1	+ 9.7	+ 13.5
Brazil	2.27	3.04	4.08	19.76	27,116.0	+1.5	+ 3.5	+ 21.1
Chile	543	640	975	4.20	9,924.0	–1.2	+ 10.7	+ 13.4
Colombia	2,293	2,609	4,119	7.03	6,955.4	+8.7	+ 60.0	+ 64.2
Mexico	10.6	11.4	19.0	9.61	14,702.6	+0.6	+ 13.8	+ 19.8
Peru	3.25	3.41	5.84	2.76	4,477.2	+0.6	+ 20.7	+ 21.7
Venezuela	2,638§	2,779§	4,741	12.22	18,874.2	–1.4	– 37.0	– 38.4
Egypt	5.77	6.19	10.36	9.40	41,906.9	–1.0	+ 70.5	+ 79.4
Israel	4.51	4.54	8.11	3.64	700.0	–1.7	+ 8.7	+ 4.1
South Africa	6.38	6.21	11.5	7.10	15,736.9	+2.0	+ 24.3	+ 9.7
Czech Republic	23.7	25.7	42.6	1.79	1,285.0	+1.8	+ 24.5	+ 17.4
Hungary	197	202	353	6.40	20,713.6	–1.4	+ 40.5	+ 29.1
Poland	3.26	3.61	5.85	4.70	31,055.3	+0.8	+ 16.6	+ 7.2
Russia	28.4	29.3	51.0	13.00	815.1‡	+4.4	+ 35.9	+ 32.7
Turkey	1.32	1.46	2.37	16.14	29,683.2	–0.1	+ 18.9	+ 21.5
EM (MSCI)*	1.00	1.00	1.80	na	622.6	+0.7	+ 14.8	+ 14.8
EMBI+†	1.00	1.00	1.80	na	348.7	nil	+ 5.8	+ 5.8

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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